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Royal Commission on Banking and Finance

The Canadian Life Insurance Officers Association.

Hearings held at

Ottawa

Vol. 24

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Toronto, Ont.

ROYAL COMMISSION ON BANKING

AND FINANCE

Hearings held at Ottawa,
Ontario, on Monday,
July 9th, 1962.

THE COMMISSION

The Honourable Dana Harris Porter
Chief Justice of Ontario
Toronto, Ontario - Chairman

Mr. W. Thomas Brown, M.B.E.
Investment Dealer
Vancouver, British Columbia

Mr. James Douglas Gibson, O.B.E
Banker
Toronto, Ontario

Mr. Gordon L. Harrold
Agriculturalist
Calgary, Alberta

Mr. Paul H. Leman
Corporation Executive
Montreal, Quebec

Mr. John C. MacKeen
Corporation Executive
Halifax, Nova Scotia

Dr. W. A. Mackintosh
Vice-Chancellor
Queen's University
Kingston, Ontario

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Mr. Gilles Mercure - Joint Secretary

Nethercut & Young
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Ottawa, Ontario,
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--- At 8.50 A.M. the hearing commenced.

SUBMISSION OF THE CANADIAN LIFE
INSURANCE OFFICERS ASSOCIATION

APPEARANCES

Mr. E. A. Rieder, - President, The Mutual Life Assurance Co. of Canada, and President of this Association

Mr. J. T. Bryden, - Vice-President and General Manager, North American Life Assurance Co., and Immediate Past President of this Association and Chairman of its Special Committee on Banking and Finance

Mr. G. L. Holmes - President, The Manufacturers Life Insurance Co.

Mr. A. Ross Poyntz - President, The Imperial Life Assurance Co. of Canada

Mr. G. T. Westwater, - Manager for Canada, The Standard Life Assurance Co

Mr. E. R. Alexander - Vice-President, Finance, Sun Life Assurance Co. of Canada.

Mr. A. H. Lemmon - Vice-President and Treasurer, The Canada Life Assurance Co.

Mr. H. A. Rapsey - Financial Vice-President, The Manufacturers Life Insurance Co.

Mr. W. J. McCarthy, - Associate Treasurer, Sun Life Assurance Co. of Canada.

Mr. E. H. Crawford - Assistant Treasurer, The Canada Life Assurance Co.

Ottawa, Ontario,
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Mr. [illegible] - [illegible] The Standard Life Assurance Co.

Mr. [illegible] - Vice-President, [illegible] Sun Life Assurance Co. of Canada.

Mr. [illegible] - Vice-President and Treasurer, The Canada Life Assurance Co.

Mr. [illegible] - [illegible]

Mr. [illegible] - [illegible] Sun Life Assurance Co. of Canada

Mr. [illegible] - Assistant Treasurer, [illegible]

Mr. J. N. Falkner - Associate Investment Officer, Prudential Insurance Co. of America.

Mr. John A. Tuck, Q.C. - Managing Director and General Counsel, The Canadian Life Insurance Officers Association

Mr. James B. Clinton - Investment Department, North American Life Assurance Co.

Mr. Frank C. Dimock - Secretary of the Association,

THE CHAIRMAN: I call the meeting to order. Today we have a submission from the Canadian Life Insurance Officers Association. I understand that Mr. Rieder will open the discussion.

I may say that we have all read with very great interest the brief which had been filed with us by your Association and it is indeed a very comprehensive and illuminating brief. We appreciate very much the great amount of work which must have been put into its preparation. We are sure it will be of very great assistance to us.

Now, I will ask Mr. Rieder to begin. If any of you gentlemen wish to remain seated while addressing the Commission it is quite all right.

MR. RIEDER: Thank you very much, I will take advantage of your kind offer. My name is E. A. Rieder, and I am president of the Mutual Life Assurance Company of Canada. I am appearing before the Commission this morning as president of the Canadian Life Insurance Officers Association, a voluntary organization consisting of 100 companies in the life insurance business in Canada. The

Association provides a forum for the examination and consideration of the problems of the procedure of the companies, the procedure followed by these companies in the past and to make recommendations to its member companies which they are free to accept or object.

These 100 companies have in force in Canada $50 billion in life insurance representing about 99 per cent of the total amount of life insurance in force to Canadians. These amounts cover nine million Canadians of every particular status in Canada and include $8½billion in investments and reinvestments each year amount to approximately $1-3/4 billion.

My responsibility is to introduce to you the representatives of our Association particularly those who have been closely involved in the preparation of our submission. They are prepared to answer the questions which the Commission may wish to direct to us.

The Chairman of the Special Committee which is appointed to prepare the submission and its chief architect is Mr. J. T. Bryden, Vice-President and General Manager of the North American Life Assurance Company.

We believe our Association has been singularly fortunate to have Mr.Bryden's knowledge of the Canadian financial system available to us. He will introduce our submission and act as our chief spokesman.

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The names of the members of our special committee which was charged with the duty of preparing this brief appear in the appendix and six of these members are with us this morning plus the secretary.

I would now like to introduce to you my colleagues and in addition to Mr. Bryden who is, by the way, the immediate past president of the Life Insurance Officers Association, is Mr. G. L. Holmes, the president of the Manufacturers Life Insurance Company. Will you signify by raising your hands as I call your names?

Mr. A. Ross Poyntz, president, The Imperial Life Assurance Company of Canada on my immediate left, Mr. G. T. Westwater, manager for Canada of the Standard Life Assurance Company in Montreal, Mr. A. H. Lemmon, vice-president and treasurer, The Canada Life Assurance Company of Toronto. Mr. Hugh A. Rapsey, Financial vice-president, The Manufacturers Life Insurance Company, Toronto. Mr. W. J. McCarthy, Associate Treasurer, Sun Life Assurance Company of Canada in Montreal, Mr. E. H. Crawford, Assistant Treasurer, The Canada Life Assurance Company, Toronto. Mr. J. N. Falkner, Associate Investment Officer, The Prudential Insurance Company of America, Toronto, Mr. John A. Tuck, Q.C., Managing Director and General Counsel, The Canadian Life Insurance Officers Association.

In addition we have here Mr. James B. Clinton

of the Investment Department of the North American Life in Toronto and Mr. Frank C. Dimock, Secretary of the Association. Both of these latter two had the responsibility for the physical preparation of the submission.

Before Mr. Bryden takes over, may I say how welcome the deliberations of this Commission have been to our industry, particularly in view of the stresses and strains which have become apparent in Canadian financial affairs during the last few years. The life insurance industry has always been an important factor in the Canadian financial system, and we are vitally concerned with that system's health and efficiency. As an Association we have been happy to provide you with information about our industry and its activities which will assist you in your most important task.

Now, the information provided in our submission deals primarily with the federally registered life insurance companies but includes information on the provincially chartered companies wherever available, but does not include the fraternal benefit societies.

Our brief has bean arranged into five main sections plus an introductory page and a summary section on blue paper.

The first is a general prescription of the life insurance business, the second section is a more detailed description of the business from the

standpoint of savings, the third section is an even more intensive description of the investment operation, section four is a consolidation of the Association companies' views on fiscal and monetary policy and finally, the Associations companies' views on the organization of the capital market in Canada.

Now, I would like to turn this introduction over to Mr. Bryden who will make the main presentation.

THE CHAIRMAN: Thank you, Mr. Rieder.

MR. BRYDEN: Mr. Chairman, this brief was filed with the Commission in June and since it has received your attention, nothing would be gained by reading all or really any part of it at this time. In its preparation we have tried to bear in mind the Commission's frame of reference, and the rather exhaustive list of questions or subjects indicating areas of your special interests which were received from your staff. We have tried in this submission to indicate who we are, what we do, why we do what we do and what we think about some aspects of fiscal and monetary policy and also the operations of the capital market.

In summary we suggest first of all that the Commission might consider whether the prohibitions in the insurance acts against the investing of life insurance funds in the shares of another life company may not have militated against the retention of ownership of Canadian life insurance companies in Canada.

We suggest that the Commission may wish to consider, in the context of the capital market generally,

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We suggest that the Commission may wish to consider, in the context of the capital market generally,

the existing limits and the present standards for the year-end valuation of assets that are contained in the present legislation.

We suggest that the Commission might consider, in the light of the continuing supervision to which the life insurance companies are subjected, whether uninsured pension plans and investment vehicles through which individual accumulation under "registered retirement savings plans" should not be the subject of supervision of similar character and purpose.

We also observe that the services of the so-called bond jobber or the formation of a bond exchange would not, at this time, be particularly useful, in our opinion.

We observe that to the extent that municipal governments cannot borrow directly, some form of pooling arrangement through provincial sponsorship may be the only effective way of adding the additional credit to allow access to the capital market.

We observe that privately financed development corporations participated in by large groups of investors might be a practical way of surmounting the difficulties involved in financing new and high risk companies.

We also observe that if it were deemed desirable to supply N.H.A. mortgage insurance to existing houses, the loan should be limited to a bona fide purchaser of a single house who intends to reside in it and the loan limited to, say, 80 per cent of a lending value and subject to an amortization period that recognizes

[illegible]

the year-end valuation of a[illegible]

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fully the age of the house, its location and remaining economic life.

Then, in the brief, we express our belief that there is the highest need for the continuous coordination of monetary, fiscal, debt management and exchange policies and state that no one policy, and particularly monetary policy, can in the long run make up for shortcomings in other policies.

We express our belief that government must accept ultimate responsibility for monetary policy, but that the Bank of Canada should be accorded wide latitude in initiation and implementation until such time as the views of government and bank management cannot be reconciled.

We express our belief that the Bank of Canada should carry out its monetary policy through varying the money supply and thus influencing interest rates and liquidity. To the extent that distortions appear from time to time and correctives are deemed necessary such problems should be treated by government through temporary regulations rather than by attempting to bring non-bank financial intermediaries under some form of continuing relationship with the central bank. We believe, however, that in peace time at least, such direct controls should be considered only as a last resort. We express our belief that the Bank of Canada should give the fullest possible explanation of what it has done, should keep its emerging views and intent constantly before its Minister, but other

than that should be able to carry on its operations in reasonable anonymity.

We express the belief that any restrictions whereby life insurance companies would be required to invest a certain portion of their assets in any particular category of investment would not be in the best interest of either policyholders or the nation. Such restrictions would tend to lower arbitrarily the investment returns of those particular savers.

We express our belief that reasonable price stability along with a high level of employment and income should be the two major objectives of public policy. Just as combatting recession requires the use of a broad arsenal of weapons, so combatting inflation requires an equally broad attack not only on the monetary front but in fiscal matters and in economic policy generally.

We express opposition to proposals for the addition of the government operated compulsory pension plan providing graduated benefits on top of our present Old Age Security Plan. The use of existing pension facilities, subject possibly to minimum requirements of portability and benefit level, would continue to accumulate pools of private savings for investment through the capital market.

Now, Mr. Chairman, we have so organized ourselves that certain members of our delegation have more intimate knowledge of certain phases of our presentation and if I may, I should like from time to

time to direct your questions to one or more of my associates or ask them to supplement answers already given.

We shall be most happy to try to answer any questions that arise as a result of the brief we have submitted.

THE CHAIRMAN: Thank you, Mr. Bryden.

COMMISSIONER GIBSON: Mr. Chairman and gentlemen, I would like to ask you a few open questions about the structure of the life insurance industry and I would like to make a general comment as well which comes up in this context.

Studying your brief indicates pretty clearly that the practicesas between one company and another are by no means the same, investment practices, for example. That being the case and since our greatest interest is in finding out how you find market influence and how you fit into the financial system we would very much appreciate knowing whether, when you speak, you are speaking from your own particular experience so we can get a clear reason as to why it is done in this way and how you respond in different circumstances; in other words, as you have pointed out yourselves in the brief, in a number of places the practices are quite different in some respect, and where they are we would like to know as much as we can about why they are and how the response occurs. To start out, I would like to ask you a few questions about the nature and structure of the industry. For instance, you cover in your brief the federally chartered and

provincially chartered companies. Is there any particular striking difference in these two types of company? I notice, for example, provincial companies, although very much smaller, have, in the period which you indicate, grown a great deal faster. Is this significant?

MR. BRYDEN: Mr. Poyntz.

MR. POYNTZ: I should think a general answer Mr. Chairman, would be, that the provincially registered companies probably operate more locally than the federal ones and are probably younger companies and therefore growing more rapidly for that reason. I think a good many, for example, of the provincially chartered companies operate in the province of Quebec, perhaps entirely.

COMMISSIONER GIBSON: Is there any particular difference between large and small companies and the way they are growing in the last 20 or 25 years? Do the larger ones tend to get larger or have there been a lot of new small ones?

MR. POYNTZ: There have not been a lot of new small ones. I think we have that in the brief, the number that have entered the business recently. Twenty-five Canadian companies have entered the life insurance field between 1935 and 1960.

COMMISSIONER GIBSON: Has there been any tendency for the industry to develop in larger units through other phases of the life insurance business?

MR. POYNTZ: I do not believe that any particular range of size has been capturing a bigger share of the

[illegible]

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[illegible]

MR. SNIDER: Mr. Poyntz.

MR. POYNTZ: I should think a general answer, Mr. Chairman, would be, that the provincially [illegible] and therefore growing more rapidly for that reason. I think a good many, for example, of the provincially [illegible] perhaps entirely.

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MR. POYNTZ: I do not believe that any particular [illegible] capturing [illegible]

market. As you point out, the smaller ones have maintained their position, the provincially registered ones and have again covered about one per cent of the market, I think it is, to five per cent, in this period 1935 to 1960. The larger companies are growing but probably not at the same rate of growth. Growing the same absolutely, but not at a greater rate.

COMMISSIONER GIBSON: What about the distinction between Canadian owned, British owned, American and other companies? Are there any characteristics of each group on the present ownership? Are there differences in asset management, for example, that you would say are characteristic of British companies, American companies and Canadian companies?

MR. POYNTZ: Yes, I think there are some differences in asset management that could be found in some of the British companies. Mr. Westwater represents one of them and I think probably he might be able to answer that question.

MR. WESTWATER: Mr. Chairman, I would refer you to Section 5 where we point out the marked differences in distribution of assets and a different investment policy between the British and Canadian companies --

COMMISSIONER GIBSON: This is as between the Canadian operations of the British companies and Canadian companies? Now, you do point out that the British companies' practices in the United Kingdom are different.

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MR. WESTWATER: Yes sir, that is an important point. I should say that within the limits of the federal restrictions and regulations here the British companies would follow a similar line of policy in Canada. There are, of course, limits.

COMMISSIONER GIBSON: In other words, they would tend to hold more common stocks than Canadian companies?

MR. WESTWATER: Yes.

COMMISSIONER GIBSON: Is there anything in particular about American companies and the way they operate here that differentiates them in any way?

MR. POYNTZ: Well, for their Canadian business specifically they must follow the same line as the Canadian companies. There are a good many U.S. companies operating here, mainly an investment operation rather than a life insurance business and, of course, they would not necessarily have the same investment management for that. Possibly Mr. Falkner would like to reply. He represents one of these United States companies.

MR. FALKNER: I cannot add much to what already has been said. I think it would be a fair statement that we operate investmentwise in a manner similar to our Canadian competitors, possibly with a little different emphasis in the Canadian structure of Prudential in the type of investment we favour. So far as Prudential is concerned it is generally our mortgage investments that are at the moment most attractive.

COMMISSIONER GIBSON: You put more emphasis on mortgages relative to bonds?

MR. FALKNER: In Canada, yes, and this I would say is purely on account of or mainly on account of our organization. We are best equipped for this particular type, I feel, to participate in that form of investment.

MR. POYNTZ: I am sorry, Mr. Chairman, could I refer back to the previous question of yours dealing with the rates of growth of various types of companies? It is covered in paragraph numbered 3.56:

> " Competition within the industry is further indicated by the decline in the share of life insurance in force held by the larger companies. For example, in 1935, the five largest companies held 53% of the business in force; in 1960 these same companies held 48%. The next five companies had on their books 24% of the total life insurance in force in 1935, in 1960 these same five companies held 19% of the total. In 1935 the largest share held by any one company was 16½%; in 1960 the largest company, which had been third largest in 1935, had 12%."

I am sorry to interrupt your chain of questioning.

COMMISSIONER BROWN: This would happen anyway if more companies entered the field. Obviously, the percentages are going to go down.

MR. POYNTZ: That is true.

COMMISSIONER BROWN: Have you figures for the relative rise in growth within that same grouping?

MR. POYNTZ: I do not think we have.

MR. RAPSEY: We have some absolute figures here. We have not quite worked out the relative rate of growth, for example, a company that stood at the top in 1935 had $1 billion on the average. At the end of 1960 it had $5.3 billion. If you drop down to, let us say, the tenth company at the end of 1935 they had $200 million in force, and at the end of 1960 they had $950 million in force; in other words, about five times in one case and about four and a quarter times in the tenth case, but at the same time you will find variations either way within the ten.

THE CHAIRMAN: I assume that none of those twenty-five companies have failed during that period. Have there been any amalgamations in that group?

MR. BRYDEN: One, I think. One company took over another in 1960.

MR. RAPSEY: Not in this group of ten.

MR. BRYDEN: No, not in the top group of ten.

Mr. Chairman, may I go back to one question that Mr. Gibson raised and I think the answer on the average is found at page 80 of the brief where we list in table 5.f, life insurance assets held in Canada by federally registered companies and it is broken down as to the Canadian companies, the British companies and the United States companies and other companies and again percentages are given

[illegible]

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The only thing apropos is that as far as Canadian companies' assets, they are all shown as book values, whereas non-resident companies' assets are shown at market values, and that has some relationship to the common stock holdings.

As far as your Canadian companies are concerned, I think the market values of the stocks that were held at that point were just about double the book values that are shown. I think that sets forth the differences in the investment policy of the average of the various companies. It does mask the differences in the investment policies of individual companies which go to make up that average.

COMMISSIONER GIBSON: That does bring out a couple of points that were mentioned. The British companies hold a relatively high proportion of the common stocks, and this shows the American and other companies holding an extraordinarily high percentage of corporate bonds. Would you care to comment on that?

MR. FAULKNER: It is difficult to relate these figures to our own position and the position we might find ourselves occupying in the tables. Why it should be that way I cannot answer.

MR. BRYDEN: I think Mr. Lemmon may have some information on that subject.

MR. LEMMON: Mr. Chairman, I think part of the explanation in this regard was touched on by Mr. Faulkner in respect to the type of organization. In other words, to do mortgage business you have to have in this country a branch organization. For a company

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comping into Canada in the first instance and for many years after, the volume of business it has available does not make worthwhile the setting up of a mortgage organization. To get the maximum yield on funds without going into the mortgage field, the corporate bond area is perhaps one of the most attractive to go into. Mr. Faulkner's company and several of the other large ones do go into the mortgage business through an organization, but many of the non-resident companies have not seen their way clear to do that. Therefore this is sort of the residual area, corporate bonds.

The Chairman has called my attention to the fact that some of the American companies are very highly geered to do a direct placement business with corporations. They have carried that over into this market using their American organization to do it, which also contributes to the higher percentage of mortgage bonds.

COMMISSIONER GIBSON: There must be a number of large ones that do this on a big scale.

MR. LEMMON: That is one large one which does it on a very substantial scale.

COMMISSIONER GIBSON: We have been talking a bit about the characteristics of different owned companies in assets management. How about the type of business they take on? Do British companies have different characteristics than Canadian companies? Do they sell particular kinds of insurance more than Canadian companies, or is the mixture different? Do the American companies tend to specialize in particular fields?

MR. BRYDEN: Mr. Chairman, maybe I stand subject

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COMMISSIONER GIBSON: We have been talking a bit about the characteristics of different owned companies in assets management. How about the type of business they take on? Do British companies have different characteristics than Canadian companies? Do they sell particular kinds of insurance more than Canadian [illegible] [illegible]

MR. BRYDEN: Mr. Chairman, maybe I stand subject

to correction here, and if I need to be corrected I trust someone will do so. I would think that on balance the normal life insurance business of the United States companies, of the Canadian companies, and to eme extent the British companies, are reasonably well the same. There are some companies within the different groups that tend to specialize to a greater extent on annuity business rather than the insurance business. Some others are not carrying the same proportion of annuity business, but on balance, I would think that on the whole the mix is not too different. Mr. Westwater, would you agree with that or not?

MR. WESTWATER: I would agree with that answer, yes.

COMMISSIONER GIBSON: In other words the kind of business is not particularly related to the place of ownership or the origin of ownership?

MR. BRYDEN: No, your kind of business is really related to the market in this country for your particular product.

COMMISSIONER GIBSON: Is there a good deal of specialization among the companies regardless of where they are owned? Do some specialize heavily in one type of insurance and others in other types?

MR. POYNTZ: Not generally speaking, Mr. Chairman.

MR. BRYDEN: Again I think you have to tailor your product to the market, and on balance pretty generally you are going to get the same type of mixture of business that you do with the exception that some

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companies do specialize to a greater extent in annuity and group pension business than others.

COMMISSIONER GIBSON: You are speaking of the larger companies. I am wondering if there are any small companies for instance non-life companies, that go into the life businesss in order to supplement their own business and thereby specialize in a certain area.

MR. POYNTZ: This has not happened in Canada very much.

MR. RIEDER: There is one difference that should be mentioned I think in answering your question.

There are four large companies operating in Canada which do what was formerly called industrial business; that is, going around to collect premiums weekly or monthly at the house. That class of buyer is a different type of person than is being sold by the majority of companies. However, that type of business is becoming less and less significant with the rising standard of living even among the industrial workers.

COMMISSIONER GIBSON: How about new companies starting up, do they tend to go into the general business, or tend to specialize in some particular operation?

MR. RIEDER: I think we all do all kinds of business with the exception of accident and sickness insurance. Of course, perhaps half the companies are in that field and half are not. As far as life insurance and annuities are concerned, we are all selling everything.

COMMISSIONER GIBSON: Some do more group than

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COMMISSIONER GIBSON: Some do more group than

others. Would a new company starting up go into group seriously, for example?

MR. POYNTZ: There has been an example of that. A company has gone into the group field extensively right from the beginning. I do not think you can generalize really. I think also it can be said that a new small company would not likely do much annuity business.

COMMISSIONER GIBSON: Thinking again still of the characteristics of the industry, what about profitability? Do the larger companies tend to be more profitable than the smaller or vice versa, or are some kinds of business more profitable than other kinds?

MR. BRYDEN: Have we got an actuary present?

MR. POYNTZ: Mr. Holmes could explain that.

COMMISSIONER GIBSON: Perhaps I should go a little further. Do companies tend to concentrate their activities in more profitable kinds of business?

MR. HOLMES: I would say Mr. Gibson that the larger companies are bound I think to have very widespread organizations which do a general business. Most of the smaller companies enter that field when they go into it because they are entering usually with small men in their individual sales programmes. We try to find the most profitable fields, of course, but you have to take a look at your selling business and find the most profitable field. If you think there is more profit in one kind than in another you make a more extensive effort in your selling with the result that you probably lose the profitability, but you get the business.

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COMMISSIONER GIBSON: I was just wondering about the group field in the business. I have heard that it is a pretty competitive field but companies seem to be very vigorously competing in it even though it may not be the most profitable kind of business. There seems to be a general tendency to try to get in it in every department.

MR. HOLMES: Taking our own company as an example, we have not been very active in the group business, although the eagerness of the others to get into it may make us think we have made a mistake.

COMMISSIONER GIBSON: You put qite a lot of emphasis on volume in the insurance business. Do you do this just for the sake of getting more volume on your books?

MR. HOLMES: I think we may tend to do that a little in that as long as I have been in the business volume has been one of the main criterion of size. I think this is losing that effect. At one time the business was pretty uniform and volume was a pretty fair indication of what the company was doing. Today that is not the case, and I think that is recognized.

COMMISSIONER GIBSON: You are tending to look more for premium income rather than the amount of insurance in force?

MR. HOLMES: Yes.

COMMISSIONER LEMAN: Mr. Gibson, are we going to take it for granted that group business is less profitable? Why don't we ask a question in that regard.

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COMMISSIONER LEMAN: Mr. Gibson, are we going to take it for granted that group business is less profitable? Why don't we ask a question in that regard.

Is it or is it not, after you consider selling costs, more or less profitable?

COMMISSIONER BROWN: Perhaps they would each like to put in sealed and separate answers.

MR. POYNTZ: I should think we could answer that question by saying that group business is one of the most competitive fields of our operation, and for that reason margins of profit are very slim, in the group life field particularly.

COMMISSIONER LEMAN: The selling costs are lower?

MR. POYNTZ: Yes, they are.

COMMISSIONER LEMAN: If we consider that division of business right back to the question of growth which Mr. Gibson was questioning you about, what are the factors that tend to limit the rate of growth of an insurance company?

MR. POYNTZ: I think really it is a function of manpower. The size and success with which a company develops its sales force really determines its rate of growth.

COMMISSIONER LEMAN: There are no technical limitations such as accounting in respect to reserve requirements?

MR. HOLMES: There are technical limits particularly to group that tends to cut down the surplus and higher earnings, and that is why costs are higher than your growth. They tend to be that way but they are not necessarily that way.

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have not in fact limited the growth of any of the members of your association?

MR. HOLMES: I think at times they have limited us to some extent, but not a great deal. I would say normally no, you grow really as fast as you can on a reasonable basis.

MR. RIEDER: Mr. Holmes is speaking from the standpoint of a fairly large established company. I think it is true that there is no practical limitation on the rate of growth for technical reasons in setting up reserves and so on. However, for a new company that might be true; that is a small company.

COMMISSIONER GIBSON: The reason being that an insurance company does not like to see its surplus reduced to more than a modest amount in any given year, is that right?

MR. RIEDER: That is right, it has to keep some surplus, but you can eliminate surpluses entirely in small companies.

COMMISSIONER GIBSON: Because of the heavy cost of the first few years of writing policies, and because of the initial cost?

COMMISSIONER BROWN: Can you give us a rule of thumb in this regard?

MR. BYDEN: Subject to correction, Mr. Chairman, and I have about three actuaries here, it has also seemed to me, in a going concern, with the existing insurance in force it is producing surplus and earnings fast enough to let you fix a growth rate in force of between 8 and 9 per cent. Once you move

have not in fact [illegible]

company of your [illegible]

[illegible]

to a growth rate that goes much beyond that then you have what we call a surplus strain. In other words it tends to bear down on the net operating revenue which is produced in that area. That may not be significant in itself, but the mere effect of the bearing down does sometimes tend to have some effect on your dividend distribution to your existing policyholders and tends to bring that out at a level which might conceivably produce inequity to existing policyholders against the new ones. That has sort of been my rule of thumb in this regard. However, I speak subject to correction.

MR. POYNTZ: I think the only thing we might add is that there is a specific technical deterrent in the single premium annuity class of business where even for a large company the reserve requirements are stringent and quite often result in a liability being assumed that could be as large or larger than the single premium received. The difference, of course, will be made up by excess interest, but that has a very specific technical deterrent.

COMMISSIONER LEMAN: Would there be some justifiable way of accounting differently for that type of business?

MR. POYNTZ: It would involve changing the liability standard in the Canadian-British Insurance Companies Act. There has been some relief recently. The rate of interest allowed is now 4 per cent and it used to be 3½ per cent. Companies on new money can earn more than 4 per cent and can use a higher rate of

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interest in calculating the premiums but not a higher rate of interest in calculating their liabilities,so the liability is high relative to the earnings on premium.

COMMISSIONER BROWN: Do these technical factors tend to affect the type of business that a new company tries to write; for example a new company setting up, because of these technical reserve requirements on straight life insurance would then tend to try to grow faster in the group end of it rather than the straight life end of it?

MR. POYNTZ: A new company would normally have difficulty in the group field since they would not have a specialized group sales organization. I did mention one specific new company that did get into the group business quickly, but normally that is not the case.

COMMISSIONER BROWN: Is it because of the selling aspect?

MR. POYNTZ: Yes.

COMMISSIONER BROWN: But from the point of view of their accounting end of it, would there be a tendency for them to try to emphasize one type of business rather than another type because of these reserve disabilities connected with certain kinds of insurance?

MR. POYNTZ: Ithink they would tend to do what we call the normal type of life insurance business, yes.

MR. BRYDEN: I think, Mr. Brown, that one of

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the things that may happen there is that there is no doubt that there is a limit to the amount of new business that a new and small company can put on its books in any one year and still remain respectable on its balance sheet. However, I think what would happen there is, through the re-insuring facilities throughout the industry it might very well take all the new business it can sell and then, having regard to the differences in any capital and the amount of risk that it wants to assume on its own account, it might very well seed the excess business to some other carrier. I think that is one of the ways that they would tend to control their balance sheet position and the risks versus the equity that they have in it.

MR. POYNTZ: Mr. Chairman, I think this last discussion is fairly academic because the whole business of life insurance in Canada is so competitive that a company is usually trying to get as much business as it can rather than to limit the amount of new business that they do.

COMMISSIONER BROWN: That is what I wanted to know.

THE CHAIRMAN: What I have some difficulty in understanding is how these 25 companies, without any background and without very much of a balance sheet, have succeeded in competing with the big companies at the rate that I understand they have done. What is the reason for their success? Is it that they have tapped new areas of prospective customers by salesmanship?

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MR. BRYDEN: I would think that they have produced the best and most competitive rates that they can and the new company is much more likely to acquire business through what you might call brokerage connections without doing what a lot of companies do, and that is have their own carrier life underwriter agency force. I think they might pick up bits and pieces in a fair amount. And that is one of their methods, I think, of breaking into the matter and getting a fair amount of business on their books, so it is partly the method of how it is sold or through whom, rather than any particular mix in what is sold.

MR. RIEDER: A lot of these companies are Quebec provincial companies, are they not, which have a special field in the province of Quebec.

MR. BROWN: You mentioned reinsurance; are there some of those that specialize in reinsurance or do all companies?

MR. BRYDEN: There are specialists.

MR. POYNTZ: Yes, there are specialists, in reinsurance, but most -- certainly all the larger Canadian companies will do reinsurance as well.

MR. BRYDEN: Each company will normally have a retention limit on any one policy having regard to the total of their reserve liabilities. And, for example, I can at the moment say that ours was $100,000 a policy and in excess of that we would reinsure the excess part with some other company and in that way you do not control the risk on individual policies and that would be common, I would

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say, right through the industry; in other words, each company has its own retention limits, but that does not prohibit it from writing larger policies.

THE CHAIRMAN: And the smaller company has the smaller risk?

MR. BRYDEN: Yes.

THE CHAIRMAN: But they still have the reinsurance facilities open to them.

MR. RAPSEY: The bulk of the reinsurance is passed to the companies and some of the smaller companies tend to use special reinsurance facilities but both are available and the smaller company can go to the larger company and get reinsurance.

MR. BROWN: Are there any Canadian companies that specialize in reinsurance?

MR. BRYDEN: There is one Canadian company, I think, and the rest of them pretty well are foreign companies.

MR. POYNTZ: The Canadian reinsurance companies, I know the name of one that does specialize in it but it is owned by foreign interests.

COMMISSIONER BROWN: There is none Canadian owned?

MR. BRYDEN: Not that we know of.

COMMISSIONER GIBSON: Still on the nature of the industry, you do not say very much about the foreign business of the Canadian life insurance companies in your brief, and I wonder if you care to make a comment. This is from the Canadian point of view and there may be a certain amount of money which is coming back to

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Canada from connections abroad.

Now, looking in the Bank of Canada annual statistical supplement, it shows quite substantial net annual transfers in funds from abroad on the part of twelve life insurance companies, and they include some large Canadian owned ones, and these show quite considerable transfers. It only goes up to 1960, but they show quite substantial transfers from abroad to Canada. Now, I wondered about this $13 billion and I wonder if you would care to comment on this. This obviously isn't going to be all profit and some of the companies are utilizing some of the funds they get from abroad. Could you develop this a bit?

MR. BRYDEN: Possibly we can take it in stages. It is first mentioned on page 18 in paragraph 3.4 and it says that there are 14 of the Canadian companies that do business outside of Canada, and at the end of 1960 they had $13 billion of life insurance in force; that equals 42 per cent of the business of those 14 companies, and that the business outside, which is 70 per cent, is on the lives of policyholders in the United States, 16 per cent in the United Kingdom, 2 per cent on Asians, 6 per cent on Africans and 6 per cent on persons in the Caribbean area.

COMMISSIONER GIBSON: We realize that your business is balanced abroad, but we are interested in the effect of the Canadian position, to what degree these funds are in Canada. These figures I quoted, would these give us a fair idea of the net operations of Canadian insurance companies and their effect on the Canadian

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balance of payment.

MR. BRYDEN: I think from that point of view that Mr. McCarthy may have some comment to make.

MR. McCARTHY: I would say, Mr. Chairman, that this is correct, that that pretty well gives you the measure of the impact on the balance of payments which, as you see, has a positive effect in so far as Canada is concerned.

COMMISSIONER GIBSON: That would be part of the profits and partly the funds throughout Canada that are used?

MR. BRYDEN: And partly an estimation of cost on the foreign business which is incurred in Canada in your head office administration, so that is a part of it, too.

MR.McCARTHY: In the last three or four years there have been, on the part of some of the Canadian companies, particularly those doing a fair sized business in the United States, a tendency to remit some portion of their surplus funds into Canada, largely on the basis of the interest rate differential and to some extent, perhaps, a concern or an awareness of the fact that U.S. taxation arrangements may take an adverse portion with regard to these surplus funds.

COMMISSIONER GIBSON: And the factors affecting this movement are the exchange differentials -- I mean, the interest rate and the exchange rate between Canada and the United States, or is there much movement from the sterling countries?

MR. McCARTHY: To Canada?

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MR. BRYDEN: I think from that point of view [illegible]

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MR. McCARTHY: To Canada?

COMMISSIONER GIBSON: Yes.

MR. McCARTHY: As far as Canadian companies are concerned, I do not think so; as far as our company is concerned, no, but on the part of the British companies I could not say.

MR. BRYDEN: I think we should bear in mind, Mr. Chairman, that all the companies attempt to match, as far as possible, their assets in a particular currency and also the liabilities. In the United States, for example, assets secured from U. S. reserves, of course, are trusteed in the States and in part I think that all of us attempt to hold a bit of a surplus over and above actual requirements. I do not believe that in the sterling area the same trusteeship prevails, but on the same basis I think all of us attempt to carry pretty well our U.K. sterling reserves in sterling currency and I think that also applies to your business in the Caribbean area, and so on, so that any movement of this kind that does occur is a very surplus type movement, a very marginal movement of funds across the border.

MR. POYNTZ: I think that this is the key to the question and that we can only talk in terms of the flow of the surplus funds and although there is substantial business done abroad by Canadian companies it will never be a big factor in the flow of funds to and from Canada because we must think only in terms of the surplus earnings and the extent of the home office operations with respect to that business.

COMMISSIONER GIBSON: There is a little more said

concerned, I do not think so; as far as our company is concerned, no, but on the part of the British companies I could not say.

MR. BRYDEN: I think we should bear in mind, Mr. Chairman, that all the companies attempt to match, as far as possible, their assets in a particular currency and also the liabilities. In the United States, for example, assets secured from U. S. reserves, of course, are trusteed in the States and in part I think that all of us attempt to hold a bit of a surplus over and above actual requirements. I do not believe that in the sterling area the same trusteeship prevails, but on the same basis I think all of us attempt to carry pretty well our U.K. sterling reserves in sterling currency and I think that also applies to your business in the Caribbean area, and so on, so that any movement of this kind that does occur is a very surplus type movement, a very marginal movement of funds across the

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in the brief on page 72 on this point, and it says that Canadian life companies have from time to time been prepared to accept some exchange risk and that the differential in interest rates appear unduly now, and that some reversal of that position occurs when the yield spread widens appreciably. Is it your suggestion that there is a certain capital flow back and forth here? Would not that be because of surplus funds?

MR. POYNTZ: It all has to be under surplus funds as far as United States and Canada is concerned. It has to be under surplus funds.

THE CHAIRMAN: Would it not be true that this paragraph, referring to the influence of exchange rates, simply does not apply to the results of your foreign business and may affect to some effect the investments arising out of Canadian business?

MR. BRYDEN: Yes, it could. We very deliberately used a word there, Mr. Chairman, "to purchase non-resident investments"; I do not think as far as I know that any of the companies are likely to take cash from here to put it there, but you do have a tendency, even on Canadian accounts, at times, if your yield spread is wider than normal, that you may move over and buy the investments and sometime later you may bring it back if the spread changes, but again we are still dealing on balance with very surplus funds, and there is no method of removing large amounts of Canadian assets that you are holding against your Canadian reserves over in the States and then back.

COMMISSIONER LEMAN: I do not want to labour this

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COMMISSIONER LEMAN: I do not want to labour this

point too much, but do not you think that if you read paragraph 5.44 that on the face of it it seems to be contradictory; it seems to say that one would expect the exchange risk and the threat of interest rates is unduly narrow, and it would seem to make more sense if it were exactly the opposite.

MR. McCARTHY: I think the writer had in mind the interest rate spread between Canada to the United States, which historically is wide in favour of Canada, but when it narrows down to where you get American rates almost at the same as Canadian rates, you might go out at a narrow spread and come back at a wider spread, or at a time when the spread is restored to something like it was restored to before.

COMMISSIONER LEMAN: It would be the opposite for movements between sterling countries?

MR. LEMMON: Yes.

COMMISSIONER LEMAN: You cannot take the paragraph just as it is.

MR. BRYDEN: No, but if, for example, the normal rate spread between Canada to the United States may be a half per cent in yield, the point at which that was a quarter spread you might very well move to the United States and at the point which it was three-quarters spread you probably would come back here.

COMMISSIONER LEMAN: Would that mean that the insurance companies in general have views on what the spread should be or what the normal spread is?

MR. BRYDEN: We know what the historical spread

has been.

COMMISSIONER BROWN: On this question of foreign assets, I notice that the Canadian companies have $13 billion in life insurance in force outside of Canada and the foreign companies have something like $14 billion in Canada and the Canadian-held assets abroad are $2.8 billion as against the foreign assets in Canada of $ 2.2 million. Does this reflect a difference in the policies they are writing? In other words, foreign companies tending to write more group policies than life policies?

MR. HOLMES: The group policy as a rule, but the Canadian will have done more abroad than the foreign companies have done here.

COMMISSIONER BROWN: So, there is a difference in policy type written by the foreign companies as against Canadian companies?

MR. POYNTZ: There is a difference in the markup which they ask. For example, Canadian companies are not extensively in the British market where the type of insurance selling is higher premium, a high premium type and therefore higher reserves than possibly it would be in the case of Canada or the United States, so that if a foreign company does business in Canada it is doing it in our market at a lower premium level than we do, say, in the British markets.

COMMISSIONER BROWN: But 70 per cent of the Canadian business is in the American market?

MR. POYNTZ: Yes. I think the group answer is quite pertinent there, that the U.S. companies do a large group business in Canada and they produce relatively

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COMMISSIONER BROWN: [illegible]

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low assets.

COMMISSIONER MACKINTOSH: What about industrial insurance; do not the American companies sell a fairly large amount of industrial insurance?

MR. RIEDER: But it is a very small factor on the total amount of insurance in force; the age of the business has some bearing on the ratio of the reserve to the face amount of the policy.

COMMISSIONER GIBSON: This brings us back to the point I was going to get at earlier; it is the amount of funds that the company nets as a result of all the activities, and shouldn't there be deductions for foreign companies who are sending funds out of Canada, and this would include three of the large foreign owned companies, but in veiw of the fact that there were a shade more in Canada of the foreign controlled companies as against insurance written outside of Canada by Canadian controlled companies, it does seem a little surprising to have as big an influence of funds to net to Canada as the figures would suggest. It would suggest something like $20 million a year net, and it seems to me that the companies are working in a more profitable area of insurance.

MR. POYNTZ: I think that some of that inflow is for the investment of, say, U.S. companies with respect to their U.S. business. Their Canadian investment accounts for the U.S. business.

COMMISSIONER GIBSON: Maybe that has not been moving quite so strongly in the last year.

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COMMISSIONER BROWN: Is there any difference in

taxation for a foreign company operating in Canada as against a Canadian company operating in Canada?

MR. POYNTZ: Not with respect to the Canadian business of each.

MR. BROWN: I would like to move into a slightly different area but still within the structure of this. One of the most obvious or most striking developments in recent years has been the mutualization going on in some of the largest companies. What was the motivation for this?

MR. BRYDEN: Well, Mr. Holmes, would you like to answer that one?

MR. HOLMES: I think the motivation was for various reasons, but they came to one point, and I think in our own company -- I will speak of it because I know it more thoroughly -- in our own company almost half the stock was held in one hand, you might say, and it was a question of that particular party deciding that they did not want the price that was quoted on the stock, they did not want to hold that much in one hand; it was in a State and rather than have that control of the company go to unknown sources, we were very anxious to have it mutual.

COMMISSIONER BROWN: How about other companies, because there are five of them?

MR. BRYDEN: Mr. Lemmon?

MR. LEMMON: Mr. Chairman, in our case the situation was not quite the same as in the Manufacturers Life. After the legislation was passed at Ottawa, a committee of the policyholders of our company set up to

[illegible] company operating in Canada as [illegible]

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MR. LEMMON: Mr. Chairman, in our case the [illegible] the policyholders of our company set up to

inquire as to whether or not it was a profitable transaction for the policyholders of the company to acquire the stock and after exhaustive analysis they arrived at a figure at which they felt that the acquisition of the stock of our company was in the interests of the policyholders. In other words, we met with some of the largest stockholders to see if, in fact, the stock could be acquired in that area and experience proved that it could be so acquired and was so acquired. The prime motive there was that for the long haul we felt it would be in the interests of the participating policyholders if the stock could be acquired at that price. If it had been somewhat higher it probably would not have been done.

MR. BRYDEN: As you know, we went through this process in 1931. We were one of the original mutualizers, but the point at that time is there was danger of the control of our company moving outside, and we at that point had a provision in our original charter which allowed the redemption of our guarantee fund, and I think it was 1931 that, in effect, our participating policyholders acquired that guaranty fund and we became a mutual company at that time.

COMMISSIONER BROWN: You mentioned the question of avoidance of external control: In this mutualization, who has control of the company -- who has votes?

MR. BRYDEN: The participating policyholders.

COMMISSIONER BROWN: And on what basis are the votes?

MR. BRYDEN: Mr. Tuck, have you got the insurance Act there?

MR. TUCK: It is generally one vote per policyholder.

COMMISSIONER BROWN: It does not relate to the size of the policy?

MR. TUCK: In some companies it related to the size of the policy.

MR. BRYDEN: But pretty generally, I think it is per policyholder of a certain minimum amount.

MR. TUCK: I think the minimum is $3,000. This is a case where the general Act does not give the whole picture, and charters do vary quite a bit. I think there are about eight or nine charters where there are variations from the general rule of one vote

MR. [illegible]: As you know, we went through this process in 1951. We were one of the original mutualizers, but the point at that time is there was danger of the control of our company moving outside, and we at that point had a provision in our original charter which allowed the redemption of our guarantee fund, and I think it was 1951 that, in effect, our participating policyholders acquired the [illegible] fund and we became a mutual company at that time.

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per policyholder -- isn't that so -- the general rule?

COMMISSIONER LEMAN: Is it per policy?

MR. TUCK: Every person contracted with the company for a participating policy shall be a member and entitled to vote.

COMMISSIONER BROWN: Should this be standardized, in your opinion, in the Act so that it is laid down how the control is governed of mutual companies?

MR. TUCK: We had a proposal to that effect under discussion with the government last year, and I think all companies were prepared to see this general rule override their charter, but there was one company which was rather anxious to maintain its special rule, and that project of unification broke down.

COMMISSIONER BROWN: Apparently there is almost unanimity but not quite in opinion on this -- or there was. Let us carry it further: Should there be anything so that a majority of directors have to be Canadians?

MR. TUCK: There is now in the Act.

COMMISSIONER BROWN: That is in the Act, is it?

MR. TUCK: Yes.

COMMISSIONER BROWN: That a majority of directors ---

MR. TUCK: I think there are two rules: The majority of the board must be Canadian citizens ordinarily resident in Canada, and the second rule is that the majority of policyholders directors must also be Canadian citizens resident in Canada.

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COMMISSIONER BROWN: In other words, it applies to both.

MR. TUCK: The total board and to the policy-holders directors.

MR. BRYDEN: In a stock company you have both types of directors: You have stockholders directors and policyholders directors.

COMMISSIONER LEMAN: Is it per policy or per policyholder?

MR. BRYDEN: Holder.

COMMISSIONER LEMAN: Does each policy give a vote? If a man holds four policies in a company, does he get four votes?

MR. TUCK: The general rule is one vote.

MR. LEMMON: In our company it is one vote.

COMMISSIONER LEMAN: Because I have three or four proxies from one company.

MR. LEMMON: Yes.

MR. BRYDEN: It is a matter of the machining.

MR. LEMMON: Don't try to vote them all.

THE CHAIRMAN: What sort of machine -- a voting machine?

MR. BRYDEN: Usually it is an Addressograph or IBM.

COMMISSIONER BROWN: Even in a mutual company there is a distinction between participating policy-holders and ordinary policyholders?

MR. BRYDEN: Let us use it -- "non-participating policyholders". It is the participating that vote, not the non-participating.

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MR. POYNTZ: I think there are exceptions to that rule.

MR. TUCK: I think in every company a participating policyholder is a member of the company. That is universally true. I think there are one or two or more -- there are a few instances where non-participating policyholders are members of the company.

COMMISSIONER BROWN: Are these mutual companies?

MR. TUCK: Yes, but this is a minority. This is what happens when charters are established years ago -- over 100 years ago in some cases -- and the general statute has gradually replaced parts of these charters, but it has not replaced them all, so some of these differences still remain.

THE CHAIRMAN: The holder of a policy of $100,000 would have one vote, and the holder of a policy of $1,000 would have one vote?

MR. TUCK: Yes, that is the general rule.

MR. POYNTZ: There is usually a minimum of $3,000 or $4,000 required to vote.

COMMISSIONER BROWN: This is in the company charter?

MR. TUCK: Yes.

THE CHAIRMAN: But there is nothing in the Act that would prevent a different arrangement if the company wished to amend its charter?

MR. BRYDEN: You have to get legislation to do that.

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THE CHAIRMAN: Yes, but it is not in the Act that the one vote per holder rule is laid down?

MR. TUCK : In the general statute, yes, it is.

THE CHAIRMAN: Is it?

MR. TUCK: Yes, and this general statute applies except where there is a conflict with the special charter.

THE CHAIRMAN: The Act provides that changes can be made in the charter of the company through a special charter -- are you talking about a special Act?

MR. TUCK: I am sorry, I should have prefaced this by saying that all of the Canadian federalcompanies are created by special Act.

THE CHAIRMAN: I see.

COMMISSIONER BROWN: I would like to switch to another point. You brought out in your submission you would like to have considered the prohibition of one company owning another company in Canada. In the Act as it stands, has there been any prohibition against amalgamations?

MR. POYNTZ: Not in the Act as it stands, but there would have to be approval by the Superintendent of Insurance and probably other cabinet ministers as well, and it has not really been up for consideration for a good many years except the one we mentioned in 1960 where a small stock company did take over the business of a much smaller mutual company.

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We feel that the Commissioners might consider

this question of prohibition of a life company owning the shares of another because the same considerations apply to an extent as made it desirable to provide mutualization machinery. There is always the question of control of the Canadian companies passing outside of Canada, and, as the brief mentioned, it has happened seven times in recent years -- seven times since 1954. We feel that some of these transfers of ownership outside of Canada could probably have been prevented if the Canadian life insurance company had had the power to buy shares of another life company, and we think the safeguards should be the same as they are at present when approval must be gained for mutualization from the Superintendent of Insurance, the Minister of Finance and the Treasury Board. These same people could authorize the purchase by one life company of the shares of another to make sure that the public interest was being served.

COMMISSIONER BROWN: Could you give us the philosophy behind why this prohibition is in the Act?

MR. POYNTZ: It has been there for many years and I expect it was originally to prevent the concentration of power, but there now being so many companies in the field -- over 100 -- that there is very little danger now of concentration of power through one company acquiring the shares of another. There are only 42 Canadian stock companies, so that even if they all merged into one there would still be 80 companies operating in the field in Canada. So that the

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original philosophy, I do not think, should hold now.

There is one other minor point: It could be useful for Canadian companies to own their foreign business in separate companies. At the present time that is not possible but we do run into certain jurisdictional difficulties in some of the areas in which we have been doing business, and it could be very useful to have segregated that business into a separate company rather than have it part of the whole. I might mention Cuba as a difficult area now.

MR. BRYDEN: And British Guiana. I think Mr. MacGregor in his annual report for 1959 went to some length to explain the Department's position relative to this matter of acquisition of other companies.

COMMISSIONER GIBSON: The essence of it was the point Mr. Poyntz made?

MR. LEMMON: Subject to correction, if my memory serves me right, Mr. MacGregor made the point if one Canadian company should acquire control of another Canadian company it was likely that the second Canadian company would pass out of existence and there would be one less carrier in the field offering policies, whereas when the control of a Canadian company is acquired by a non-resident company the Canadian company usually remains in existence as a carrier in the Canadian field and that the area of competition is not so reduced.

COMMISSIONER BROWN: This would not apply

[illegible]

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to Canadian ownership of their foreign subsidiaries?

MR. LEMMON: No, it would not. He did not cover that in his report. It was purely the combination of two Canadian companies.

COMMISSIONER BROWN: Have you discussed this with him to find out his attitude?

MR. TUCK: We have not presented anything to the Superintendent. We are aware of his views and they are reflected in the report and also in his presentation to the Senate Committee discussing the legislation of 1961. We haven't had any formal discussions with him about it.

MR. BRYDEN: This matter of having the foreign subsidiaries really has not been much of a point until recently, and I think some of our thinking there has probably come up from what heppened in Cuba. At the moment some of the companies operating in British Guiana are having a few problems, if you will, and, as Mr. Poyntz says, if you could handle these outside areas in a sort of a subsidiary company it might alleviate some of the problems you run into.

COMMISSIONER LEMAN: But it would be a Canadian subsidiary?

MR. POYNTZ: Canadian owned.

COMMISSIONER LEMAN: It would not be incorporated in the foreign country?

MR. BRYDEN: It might be.

COMMISSIONER GIBSON: On this matter of keeping Canadian ownership of the industry, it is your considered view that permitting a Canadian company

to Canadian ownership of their foreign subsidiaries?

MR. [illegible]: No, it would not. He did not cover that in his report. It was purely the combination of two Canadian companies.

COMMISSIONER BROWN: Have you discussed this with him to find out his attitude?

MR. TUCK: We have not presented anything to the Superintendent. We are aware of his views and they are reflected in the report and also in his presentation to the Senate Committee discussing the legislation of 1961. We haven't had any formal discussions with him about it.

MR. BRYDEN: This matter of having the foreign subsidiaries really has not been much of a point until recently, and I think some of our thinking there has probably come up from what happened in Cuba. At the moment some of the companies operating in British Guiana are having a few problems, if you will, and, as Mr. Poyntz says, if you could handle these outside areas in a sort of a subsidiary company it might alleviate some of the problems you run into.

COMMISSIONER LEMAN: Put it would be a [illegible]

MR. POYNTZ: Canadian owned.

COMMISSIONER LEMAN: It would not be incorporated in the foreign country?

MR. BRYDEN: It might be.

COMMISSIONER GIBSON: On this matter of keeping Canadian ownership of the industry, it is your considered view that permitting a Canadian company

to own another Canadian company's shares is the most effective step that can be taken in that direction at this time?

MR. BRYDEN: I don't think, Mr. Gibson, that the industry has a view as such.

COMMISSIONER GIBSON: No, but the Canadian owned companies might have a view.

MR. BRYDEN: But this is something we thought of in the light of the interest in the retention of ownership in Canada as one avenue that might be explored in order to keep in Canada the ownership of some of the companies whose, for one reason or another, capital stock is available for sale, and one of the major problems, of course, is that when you do attempt to put a market value on the stock of an insurance company usually, if it is a fairly significant one, you are talking in terms of a fairly large amount of money and, as you know, sometimes you don't acquire large amounts of money in Canada half as easily as somebody in the bigger markets of the United States.

COMMISSIONER GIBSON: Do you think this is a significant potential problem at this time?

MR. BRYDEN: Well, that is difficult to say, but since 1955 in seven companies, I think, control has moved outside of Canada.

COMMISSIONER GIBSON: Do you think this is likely to continue or that it will expend itself?

MR. BRYDEN: There are five of the larger stock companies have mutualized, so it is not a problem there. It is not a problem with the mutual companies;

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it is not a problem with the ones that have gone outside, but there is still a significant number of stock companies in Canada and at some point, for one reason or another, that stock is likely to come up for sale. It may be succession duty reasons or something of that kind, and at that point somebody has to underwrite it.

COMMISSIONER BROWN: There should be no distinction between the mutual company buying out a stock company as against a stock company buying out a stock company?

MR. BRYDEN: I don't think it would make any particular difference. It would lead to sort of fewer companies -- bound to -- and larger companies, and that kind of concentration always does . It is just a question of which is the better.

COMMISSIONER GIBSON: Is this the tendency in the United States -- towards larger companies?

MR. BRYDEN: I don't really know as far as the United States market is concerned. Certainly, some of our Canadian companies have been acquired by companies in the United States, but they have been left to operate as Canadian companies in Canada. I am not sufficiently familiar with the United States market to answer that question.

MR. HOLMES: There have been continual takeovers in the United States, but in the total over-all picture it is not a big thing. There are more new companies growing up than cut down by the takeovers in the last 15 or 20 years.

MR. CRAWFORD: The total number of companies

(Page 2387 follows)

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MR. CRAWFORD: The total number of companies

in the United States is growing quite rapidly.

MR. RIEDER: About 1500, isn't it?

MR. HOLMES: Yes.

COMMISSIONER LEMAN: Would foreign ownership hurt the policyholder as much with the kind of regulation there is on life insurance business in Canada?

MR. BRYDEN: On balance I would think it probably would not.

COMMISSIONER GIBSON: It is just a matter of economic control, isn't it?

COMMISSIONER BROWN: That is all.

THE CHAIRMAN: If there are no further questions on this particular subject we might adjourn for 10 minutes.

--- At this point a short recess was taken.

THE CHAIRMAN: We will now resume. Further questions?

COMMISSIONER BROWN: Mr. Chairman, just as we adjourned reference was made to one of the reasons for having a majority of Canadian directors to obtain economic control in Canada. This brings up the question of interlocking directorates of national organizations and national institutions. I am wondering if you can give us any comments as to the effect this has or does not have on such matters as the placing of group insurance, etc., or the investing in securities?

MR. BRYDEN: I think, Mr. Chairman, Mr. Lemmon has been involved in that end of the brief.

MR. LEMMON: I am not sure, Mr. Chairman, exactly what is behind Mr. Brown's question.

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MR. [illegible]: About 40% isn't it?

MR. BRYDEN: Yes.

COMMISSIONER LEMAN: Would foreign ownership hurt the policyholder as much with the kind of regulation there is on life insurance business in Canada?

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MR. BRYDEN: I think, Mr. Chairman, Mr. Lemmon has been involved in that end of the brief.

MR. LEMMON: I am not sure, Mr. Chairman, exactly what is behind Mr. Brown's question.

COMMISSIONER BROWN: There is nothing sinister.

MR. LEMMON: But there are various aspects of approach on it. As you know, a man who is a director of one life insurance company but is not a director of another and life insurance companies tend to recruit their directors from those people whom they feel can be of most value to the companies, to the policyholders from the agency point of view, from the investment point of view and from other points of view.

It is perhaps inevitable under those circumstances that people who are directors of other financial intermediaries will be invited to become directors of life insurance companies seeing that the life insurance companies are national institutions and other financial intermediaries are national institutions and the experience that makes a man valuable to one national organization makes him valuable to another national organization.

Having been appointed a director of a life insurance company to say that he is entirely disinterested in the sale of life insurance would be a hundred per cent not true. He is invited to become interested in the sale of life insurance. To what extent he uses his position as director of one company or director of another to influence life insurance I am not in a position to answer completely. In our own case we have group insurance on some companies of which our directors are also directors but there are plenty of others where we have not got group insurance.

COMMISSIONER BROWN: There is nothing [illegible]

MR. LEMMON: But there are various aspects of approach on it. As you know, a man who is a director of one life insurance company but is not a director of another and life insurance companies tend to recruit their directors from those people whom they feel can be of most value to the companies, to the policyholders from the agency point of view, from the investment point of view and from other points of view.

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As far as the investment end of the business is concerned, speaking personally I can certainly consult those directors who have knowledge and experience in certain areas when certain investments are being considered and they are asked for their best judgment affecting particular businesses. I think you would have to ask the individual directors how they solved the problem when there is a conflict of interest. I cannot answer for them. Now, is there something more on that you would like?

COMMISSIONER BROWN: No, I think that just about covers it.

MR. RIEDER: Regarding conflict of interest I think a number of companies in Canada have a regular procedure which is followed. If a director has a substantial interest in the other party to any investment transaction he has to declare his interest and refrain from discussion and refrain from the decision.

MR. LEMMON: I think that is reasonably true throughout the industry.

COMMISSIONER BROWN: I am sorry, I did not quite catch the last part.

MR. RIEDER: If a director has a substantial interest in the other party to an investment transaction or any officer he must declare his interest and refrain from taking part in the discussion or the decision.

COMMISSIONER BROWN: In other words, if an investment is being discussed in the debentures of a company in which he has a large interest he has to ---

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MR. RIEDER: He stands aside.

COMMISSINER BROWN: He does not withdraw from the meeting?

MR. RIEDER: No, he can listen but take no part in the discussion.

COMMISSIONER BROWN: And does the same apply if it is a question of somebody working out a group insurance policy in a company in which he has an interest?

MR. RIEDER: Group insurance is very competitive and it is usually placed on the basis of competitive rates, I think, rather than directors influencing. The same condition does not apply. In fact, we do not discuss group policies with our directors, the sale of group business. They are more interested in investments.

COMMISSIONER BROWN: Is there any prohibition on investments where the director has control of a company?

MR. BRYDEN: Mr. Brown, Sub-section (9) of Section 63 of the Act says:

"A company shall not lend any of its funds to a director or officer of the company or to the wife or a child of a director of officer except, in the case of a company registered to transact the business of life insurance, upon the security of the company's own policies of life insurance; nor shall a company lend any of its funds to a corporation if more than one-half of

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MR. BRYDEN: Mr. Brown, Sub-section (9) of Section 65 of the Act says:

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> the shares of the capital stock of the corporation are owned by a director or officer of the company or the wife or a child of a director or officer, or by any combination of such persons."

So there is complete prohibition under those circumstances.

COMMISSIONER BROWN: But if it is not controlled there is no prohibition, it is a question that he does not enter into it?

MR. LEMMON: Declare his interest and he does not enter into the discussion or voting.

COMMISSIONER HARROLD: I would like to turn to the individual you do business with rather than the company itself. In Section 4 you deal with life insurance savings and going down to paragraph 4.5 of page 34, I think it is, it says there:

> "... annual changes in insurance saving tend to move fairly closely with movements in disposable personal income. A prolonged economic decline tends to have a relatively heavier impact on this form of saving than it does on income while on the other hand, in periods of rapid inflation, with income rising, the increase in insurance saving tends to respond more slowly."

There is a chart on the next page, I believe, which suggests other important time-lags in the savings category and I think later on in the brief you recognize

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this and say something about the inflationary trend having something to do with personal savings but would you have any information on other things that influence investments in life insurance saving as savings at the present time, changes in individuals that would suggest what does the individual consider when he makes these purchases or savings? Is it his idea as to what is going to happen as far as he is concerned or inflation, or rise in prices of investment?

MR. BRYDEN: That is a difficult one to get at. In the first place you have a sales force who are attempting to market the products. Certainly as far as the timing is concerned periods of recession are more difficult. Periods of expansion are relatively easy. In a period of expansion such as the time when you are having significant inflation you normally tend towards the sale, I think, of more group insurance and term insurance. There is less emphasis on those plans that have a larger sized savings element. Mr. McCarthy has had a considerable amount to do with the makeup of this table. Possibly he could supplement what I have said.

THE CHAIRMAN: Is that the total down into 1935?

MR. BRYDEN: Yes.

MR. McCARTHY: I think you can summarize the answer to the question of what influences the amount of savings that the individual does through life insurance by saying that it depends on three variables. The sales force, as Mr. Brown pointed out, is an

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MR. McCARTHY: I think you can summarize the answer to the question of what influences the amount of savings that the individual does through life insurance by saying that it depends on three variables. The sales force, as Mr. Brown pointed out, is an

important one. The rating of disposable personal income as demonstrated in the table is another one and the third one and the toughest one to try to be precise about is the one I would label expectations on the part of the individual potential buyer. His expectations fall into perhaps two categories, one, his future element of money coming in the organized type plan he is buying which is future money income in a sense and perhaps also to a lesser extent he might be influenced by his expectation as to the future life of his own disposable income. If he was optimistic on his income prospects he might be a better prospect than if he was pessimistic on his future income prospects.

COMMISSIONER HARROLD: And you mentioned sales force. Does that indicate that this decreases or increases from time to time in the insurance companies?

MR. BRYDEN: The number on the sales force?

COMMISSIONER HARROLD: Yes.

MR. BRYDEN: I do not think any of us ever decreased deliberately. You are normally attempting to expand your field force. There is a fairly high turnover as far as your agency force is concerned. Some come with you and decide they do not like the selling of life insurance as a vocation; others stay with you. On balance you would be attempting almost at all times to increase your total sales force of quality, competent life underwriters.

COMMISSIONER HARROLD: How about employment trends? Does this show in the statistics at all rather than disposable income?

[illegible] The rating of disposable personal [illegible]

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[illegible]

than disposable income?

MR. BRYDEN: We have mentioned at one point here, I think 36, on page 18, that the life insurance industry had 45,500 full-time personnel in their service in Canada at the end of 1960. About 25,000 of those were in administrative positions and approximately 15,000 were full-time field representatives.

Now, that has expanded quite significantly since 1939. We did not have the 1935 figure but in 1939 we had 19,700 people. I do not believe we have that broken down between field types and administrative.

COMMISSIONER HARROLD: I am sorry, maybe I did not make it quite clear. I was thinking of the employment trend in the country as a whole.

MR. BRYDEN: I beg your pardon.

MR. McCARTHY: I should say under that heading of expectations unemployment perhaps would tend to foster in the potential policyholder a feeling of apprehension about his future income. In a high level of unemployment he would be concerned: In a low level he would not be concerned and that could have an influence.

COMMISSIONER GIBSON: On this table on page 35 there are times when the life insurance took a larger share of the disposable income, say, in the middle of the late 1930's and during the war and just after the war but really during the war these are the highest percentages in the whole picture. These were not times of particularly good expectation. There were times when I suppose competitive factors were not strong. How do you explain this? You have a level in the 1930's

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COMMISSIONER GIBSON: On this table on page 5 there are times when the life insurance took a larger share of the disposable income, say, in the middle of the late 1930's and during the war and just after the war but really during the war these are the highest percentages in the whole picture. These were not times of particularly good expectation. There were times when I suppose competitive factors were not strong. How do you explain this? You have a level in the 1930's

and during the war which is much higher than what we have had ever since the end of the war.

MR. McCARTHY: Well, during the wartime period with the lack of availability of other forms of consumption and with incomes rising very quickly and having just emerged from a period of depression people were security conscious and suddenly came into the position of being able to do something about it. That, I think, would partially explain it.

In the case of the depression period I think the ratio might be a bit misleading. I think you have to be careful in reading statistics of that sort. You will notice disposable income itself had gone down of itself. People that could afford to take care of future security in a period when this seemed terribly important to them perhaps did it more diligently and more extensively.

COMMISSIONER GIBSON: In fact the insurance policies were kept alive but the income was going down.

MR. HOLMES: That is why the ratio was higher in that period.

MR. BRYDEN: There was an attempt during a period of that kind to rather do less consumer spending in order to keep this protection in existence. It is known sometimes as inculcating the premium paying habit.

COMMISSIONER BROWN: This shows up in the figures for those years.

THE CHAIRMAN: If you look at the personal savings column there is a minus column there.

MR. BRYDEN: That was a point there, during

[illegible]

[illegible]

MR. [illegible]: Well, [illegible]

period with the lack of availability of other forms of consumption and with incomes rising very quickly and having just emerged from a period of depression people were security conscious and suddenly came into the position of being able to do something about it. That, I think, would partially explain it.

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MR. [illegible]: [illegible]

that period when there really was dis-saving.

THE CHAIRMAN: But nevertheless ---

MR. BRYDEN: They were keeping up their insurance premiums.

THE CHAIRMAN: Keeping them up surprisingly well. Of course, insurance salesmen would be at the door to persuade them to do that.

MR. BRYDEN: And do not forget on our life insurance saving figure here that is not after policy loans, that is, there were a large number of policy loans taken during this period which in turn bore down on the net saving.

COMMISSIONER BROWN: Would the same thing apply in the other direction? In the more recent period of greater inflation on group policies their net saving part of it does not apply to the same degree. Well, the same emphasis.

MR. BRYDEN: In recent years on term insurance and group insurance it has not led to a corresponding increase in the net savings because in both of those areas there are practically no reserves and no significant buildup.

COMMISSIONER HARROLD: In the case of deposits left with the company and interest how is the rate of interest decided on? Does it relate to other short-term interest rates?

MR. POYNTZ: It is related to the net interest rate which the company earns on its own assets.

COMMISSIONER HARROLD: Do these deposits show any increase in times of tight money as far as the

individuals are concerned or is it the other way round?

MR. POYNTZ: Likely the other way round.

COMMISSIONER HARROLD: You do not find any seasonal trends?

MR. POYNTZ: No, I do not think we do although Mr. Falkner had some figures on seasonal trends.

MR. FALKNER: First, we did attempt to plot and it was important to us operating in Canada to keep a fairly tight rein on the funds available for investment. We did seek to cover every avenue that brought about cash outgoing in our company and we did plot for a period of close to 20 years the Canadian conditions in policy loans and the results were somewhat inconclusive.

It appeared for a while -- you are speaking of whether we noticed any significant trend -- it appeared for a while as though people were calling upon us around income tax paying time for policy loans but in a few years that trend seemed to disappear and it is very difficult to be specific on seasonal trends for that type of borrowing.

MR. BRYDEN: Mr. Harrold, you realize, of course, that the net deposit left with the company is not a deposit account in the normal sense. It is policy deposits which are retained under option in the company for the policyholder. On Table 4.b which immediately follows the one we were talking about that gives some detail for the last 11 years. You will notice that the net deposits left with the companies in 1957 was a negative figure and also you will notice in 1959 that that was quite a point, between 1958 and 1960, and

[illegible]

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MR. BRYDEN: Mr. Harrold, you realize, of course, that the net deposit left with the company is not a deposit account in the normal sense. It is policy deposits which are retained under option in the company for the policyholder. On Table 4.c which immediately follows the one we were talking about that gives some detail for the last 11 years. You will notice that the net deposits left with the companies in 1957 was a negative figure and also you will notice in 1959

[illegible]

I think that is relative to your comment as to how that account operates during periods when money might be considered to be tight.

COMMISSIONER HARROLD: Going back to this interest rate again, you mentioned it was rated on company earnings. How often does a company change its interest rates?

MR. POYNTZ: It probably determines the rate each year. It may not change it each year but it would determine it each year.

COMMISSIONER HARROLD: With policy loans do you find that the borrowers are the younger generation or older or is there any reason that you know of that they require these loans? Is it for business purposes or what is the general reason for individuals taking out loans?

MR. BRYDEN: I think that is a pretty difficult question to answer. There is really no satisfactory method of finding out exactly what a person wants a policy loan for. It is contractual under the contract and he merely wants it, and you are under contract to provide it. So that the actual answer to that question is very difficult. I assume that some of it is used for personal reasons; emergency purposes and so on and some of it may well be for business purposes. To say exactly why they are obtained, I do not think any of us can answer with any degree of preciseness.

COMMISSIONER HARROLD: You have not put any figure on the average size of these loans either, have you?

MR. BRYDEN: I do not think we have any figures, except I think the average size of the loan is fairly small. Coming at this from another angle, one of the problems in administering policy loans is that your expenses in administering a portfolio policy loan is significantly more than that in respect to a mortgage or security portfolio. The answer that usually comes up is that because there are such a large number of small loans a lot of them may be automatic premium loans. As you know, most policies in the event that the premium is not paid go on what we call automatic premium payment until such time as it is paid or becomes lapsed. Again that is usually a small sum.

COMMISSIONER HARROLD: Would you say the repayments of these loans are responsive to the business

cycle?

MR. BRYDEN: Yes, I would think they are. Repayments were very heavy in the 1930's. Not all of them came back in cash, however. That is one of our problems. Just as a matter of interest, and this happens to be from our own position, for in Canada we had a monthly average last year of new loans to the extent of 264,000. Actually our average repayments were a little bit higher than 268,000 and of that only 95,000 was repayment in cash. Some of it was repaid out of dividends and some of it became surrenders and that is one of the big problems in the policy loan business. Some came out as matured value. However, not all of your repayments come back in cash by any means.

Mr. McCarthy, have you anything to add to that?

MR. McCARTHY: I would tend to say in pursuing policy loans as they relate to investment and availability of funds, and would direct your attention to page 45, table 4.f, you will note in the last fifteen years, or in the postwar period, that the policy loans as a percentage of the company's assets have been fairly stable around $4\frac{1}{2}$ per cent or thereabouts, quite significantly below levels that prevailed back in the 1930's when this item loomed much larger on the balance sheet.

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of these figures going back to 1890 and the trend in the 1945-1960 period has been much the same; down to around the 4 per cent level. So, as it relates to the capital market availability of funds, I would make the point that it is not or has not been, in that middle period, significant.

COMMISSIONER HARROLD: Would it be fair to say that this is a service which the companies provide rather than a form of business which they push?

MR. McCARTHY: It is a contractual right that participating policyholders generally have and the company has to keep itself in a position to go on with that commitment.

COMMISSIONER HARROLD: You do not push this as a form of utilization of assets?

MR. McCARTHY: Of course not. Company policy would be aimed at keeping the figure as low as possible.

COMMISSIONER BROWN: This comes out on the basis that net returns after expenses are lower for that investment than any other investment?

THE CHAIRMAN: Not only that.

MR. HOLMES: There is a heavier level of business on policy loans.

COMMISSIONER GIBSON: In other words, it is a perfectly secure business but you do not want to compete in the small loans area?

COMMISSIONER HARROLD: How about the interest rate on these loans? How is that arrived at?

MR. BRYDEN: The interest rate in Canada is a maximum of 6 per cent. I do not know that that is

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MR. BRYDEN: The interest rate in Canada is ... I do not know that that is

expressed in any statute anywhere, but it has been sort of the unwritten rule in the industry for a number of years. Mr. Tuck, do you have any additional information in that regard?

MR. TUCK: No, I do not think it is in the statutes, but there were discussions with the government and in parliament 25 years ago, and in the end the companies have as a matter of practice used the 6 per cent figure. It is not more than 6 per cent. The rate, of course, is put in the policy, and once it is there it is contractual, but in respect to new issues year by year it has not been greater than 6 per cent.

MR. BRYDEN: It has been as low, I think, as 5 per cent, certainly during periods when interest rates were low.

COMMISSIONER HARROLD: They have not varied too much then?

MR. TUCK: No.

COMMISSIONER HARROLD: They have stayed around 5 to 6 per cent?

MR. BRYDEN: We tend to try to let it stay at its existing rateas long as it is reasonable. At the point it becomes unreasonable we tend to move it.

MR. RIEDER: During the past thirty years it has been 6 per cent withthe exception of four or five years when we nearly all went down to 5 per cent.

MR. BRYDEN: That was during a particularly easy money era.

COMMISSIONER LEMAN: Table 4.f shows what it has been. Do you have any idea of what it could be

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MR. BRYDEN: That was during a particularly easy money era.

COMMISSIONER LEMAN: Table 4.f shows what

if everybody borrowed the maximum?

MR. BRYDEN: It could become awfully close to the total of our reserves.

MR. McCARTHY: If you went back to the American case during the high modernization period, since 1920, it has been of the order of 20 per cent. If you applied that to the Canadian picture today I think you would come up with a figure something like $1,400,000,000 of outgo.

COMMISSIONER LEMAN: That would be a bit of a mess.

MR. McCARTHY: It would be about four times, or something of that order, what we had available last year of the total. It would take us out of the capital market. I think the point should be made, however, that if those conditions arose despite the upsetting results, I think the industry would be able to handle the problem.

COMMISSIONER LEMAN: In other words, this 6 per cent is not a statutory ceiling; you could raise it?

MR. LEMMON: It is in our existing contracts, however.

MR. POYNTZ: We cannot do anything about it for existing business because the policy shows that the rate of interest will not be more than 6 per cent.

COMMISSIONER GIBSON: Going back to the question of competition with other institutions, you have a very interesting table at page 118 which shows what would happen to the assets of the savings

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COMMISSIONER GIBSON: Going back to the question of competition with other institutions, you have a very interesting table at page 118 which shows what would happen to the assets of the savings

type institutions in Canada. We took this table and tried to put it on an index basis, 1950 equals 100 because most of them start around 1950. This brings out a rather interesting point. The assets of life insurance companies have gone up a little more than double over that period; 218 roughly in 1961. This is a better record than the present savings deposits at chartered banks, but it is not as good a record as almost everything else except government annuities. It is a little better than government annuities and the Quebec Savings Bank, but compared with Canada savings bonds, trust companies, their own assets; investment companies; credit unions and mortgage loan companies -- particularly trust companies, investment companies and credit unions -- it is not as good a record although, as I say, it is better than that of the banks. Now, would you care to say anything about the thinking regarding this competition for the national savings? What are the factors that bring these varying rates about? Why are you not higher up the scale or, if you like, why are you better than the chartered banks? Is it relative to the returns on money, or is it because of inflation?

MR. BRYDEN: I think Mr. Gibson Mr. Holmes has been alerted in respect to this point.

MR. HOLMES: Mr. Gibson, my feeling would be to put it largely on inflation and the rise in the stock market in the fourteen years of that period. It has directed the minds of a number of people toward other forms of savings. It has not affected to any

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great extent the small savers who must save in dollars. It has been the background of our business but we find a tendency in the last ten years toward larger buyers of insurance. They have all bought cheap life insurance and invested their money in other places. That has been part of the reason I would say for the rise in other forms of savings, such as in trustee pensions and in a number of these trust company savings. This is based on the theory, whether it happens or not, that quite a fair chunk of that money would go into stocks which are increasing in value.

The credit union is a new development which I do not think we can put in the same class. It is a different type of development. It is a co-operative development among employees. We have them in our own companies.

COMMISSIONER GIBSON: It has to do with local circumstances and arrangements?

MR. HOLMES: Yes, but investment companies, of course, have had an effect during the last ten years on the amount of savings that have gone into life insurance.

I think if you go back to that other table that we were looking at a little while ago you will see very clearly that in poor times savings seem to be higher in llfe insurance, while in aggressive or inflationary times they tend to be not so great in life insurance.

COMMISSIONER GIBSON: Perhaps I should not ask you the next question, but what do you think the

trend is? This is perhaps asking for a business forecast, but are you going to keep up in your share of savings in the community?

MR. HOLMES: We have represented a big element in the savings element in this country, probably more so than in any other country. The life insurance companies in Canada have represented a big element. It may be that we will never be quite as big again, but I do not myself think, if we are reasonably free of inflation, that there is any reason why there should be a big change in savings in life insurance, because for most men it is the most practical form of savings.

COMMISSIONER GIBSON: Following this general picture would you say a little more about how you compete for savings? There are a number of things that you do, as I understand it, but you cannot apply more than a certain maximum interest rate. The last change was in 1961 and I believe it is 4 per cent in making your insurance calculations. You also have various choices of actuarial tables that you can make, depending on the circumstances which you think are most suitable. This has varied quite a lot depending on business forecast, but what do you do when you see that you are not keeping your share? What do you do to compete? How do you make your competition felt? Do you lower the premium? Do you allow additional earnings to go into participating dividends? What is your thinking in this regard?

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MR. HOLMES: You are thinking of the valuatio

rates on which we have to calculate our liabilities?

COMMISSIONER GIBSON: Yes.

MR. HOLMES: That has some effect but is not themajor effect on life insurance costs.

COMMISSIONER GIBSON: That is sort of a protection put in by the act?

MR. HOLMES: Yes. For instance, the rates today are double, or much more than 4 per cent in Canada. You adjust your cost in your participating business and your dividends which have been going up year by year particularly on the savings type of contracts. The valuation rate is, you might say, a minor factor in affecting the interest you actually give to the policyholders.

COMMISSIONER GIBSON: They receive participating dividends?

MR. HOLMES: In the last six or seven years there have been continuing decreases in non-participating rates and continual increases in dividends to participating rates.

COMMISSIONER GIBSON: I do not understand this point, Mr. Holmes. You are reducing your premiums on non-participating insurance as well, but you are required under the act, or at least you are not allowed to charge more than 4 per cent in making that calculation, is that not correct?

MR. HOLMES: It is a calculation of your liability on that policy, Mr. Gibson. It is not what you give the policyholder. The only place it enters into is, no matter how high the interest rate is, your

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MR. HOLMES: It is a calculation of your liability on that policy, Mr. Gibson. It is not what [illegible] into it, no matter how high the interest rate is, your

liability has to stand up. If you decrease the rate then it costs you a little more to put business on your books compared to the liability you have to put up, but it is not a major factor in regard to what you give the policyholder. It is a little check on you in giving all that the interest rate will allow, that is all.

COMMISSIONER GIBSON: So in fact you are fairly free to reduce your premium on non-participating if you want?

MR. HOLMES: Yes.

COMMISSIONER GIBSON: And do so in fact?

MR. HOLMES: Yes.

MR. POYNTZ: Could we add to this, Mr. Chairman, that competition among the companies themselves will keep premium rates as low as is practicable. We are not influenced too much, I think, in the share of the savings market in the way we move the level of our premium rates. We are influenced by the salesmanship that is employed. We have to sell the merits of our plan rather than the cost of it.

COMMISSIONER GIBSON: In other words, you have been competing in new features, and tailoring insurance requirements to individual needs and that sort of thing?

MR. POYNTZ: That is true.

COMMISSIONER GIBSON: Competition tends to take this particular form, does it?

MR. POYNTZ: Competition gets into a question of cost as between one life company and another, but as

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between our method of savings and another, it has not too much bearing. This is a service.

COMMISSIONER GIBSON: But you do think of competition in the interest rates and so on as very important?

MR. POYNTZ: Yes.

COMMISSIONER GIBSON: But when you think of competition between insurance as a form of savings and other forms of savings, you would not put rates in as being a very important factor?

MR. POYNTZ: No, because you know it will be as low as feasible anyway by reason of the competition, so you are not selling on a cost basis, you are selling one form of saving as against another.

COMMISSIONER GIBSON: But you don't put much emphasis on the sales efforts in selling insurance generally on the net interest rate a person will obtain?

MR. POYNTZ: No.

COMMISSIONER MACKINTOSH: You don't exactly whisper about the prospective policy dividends.

MR. POYNTZ: Oh, no.

COMMISSIONER GIBSON: You seem to go at this very strongly, too; when you are competing for pure savings you put this very strongly, the interest rate setup?

MR. POYNTZ: Yes.

COMMISSIONER GIBSON: But the distinction is that this isn't emphasized in the insurance side; as the saving element increases the interest rate increases?

MR. HOLMES: I think in our ordinary approach in salesmanship our salesmen approach the insurance angle first and the savings angle second; I think a great many of our men do emphasize the savings angle in the insurance sales and the approximate return.

COMMISSIONER GIBSON: What do you say yourselves as an individual company; suppose you don't think you are doing as well as you should and you should be getting a share of the savings. I take it that you

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take a look at your whole sales efforts and put on a more vigorous campaign. Can you talk about the sort of thing you do in these circumstances?

MR. HOLMES: I think personally you cut your rates if you can afford to do it. Our sales campaigns are continuous things and whether we are getting our share or not, we would like a larger share. We go at that all the time, but I think if you are running out of competition, as Mr. Poyntz says, your most obvious competition is your other insurance companies, but nevertheless you have this other competition and if you are getting out of it and you feel you can operate on a more attractive basis, you will do it.

COMMISSIONER BROWN: How fast does this reaction take place; how closely do you watch within the industry to see whether your company is keeping its position?

MR. HOLMES: It takes place very fast; we hear from our men in the field almost right away.

COMMISSIONER BROWN: You hear from them ?

MR. HOLMES: Yes, we hear from the men in the field if Mr. Poyntz puts out a rate that beats ours, we hear about it within a very short time.

COMMISSIONER BROWN: Then, how about when the industry as a whole is meeting this relative position in the competition for the savings of the public? For instance, between 1957 and 1958 the increase was not as great as it had been, but are there any major changes in policy?

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as obvious to our salesmen as the competition of the other life insurance companies but it enters into the thinking of the head office eventually. Our reaction admittedly may not be as fast to that as it is to competition with other life insurance companies, but the whole thing tends to ---

COMMISSIONER BROWN: Did you do anything between 1957 and 1958 -- was there a general change in attitude of the insurance companies?

MR. HOLMES: I don't think there is a change in that specific year, but there has been a continuous change through that whole period. I don't think there was a specific change in that year.

COMMISSIONER GIBSON: Your reaction, you say, in your company is that you have a new angle and it is to meet that competition in one way or another; either with something that is rather similar, or what do you call it if things are not going so well and you have to look at your whole sales system, or staff, or has this system changed?

MR. HOLMES: You are just talking about general company management?

COMMISSIONER GIBSON: Yes.

MR. HOLMES: Yes, you are looking at these things all the time. Sometimes you don't look sharply enough, I admit that, but you are looking at all these things; whether your men can make money and make a living on selling and that affects what you think of your compensation system, whether you are meeting the competition and that affects the cost of your policies. You have to

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think of these things all the time to find out if you are in difficulty -- if you have difficulties meeting their competition then there are certain areas where maybe you can do that, too.

COMMISSIONER GIBSON: It isn't just a question of the product, it is a question of how well you sell it.

MR. HOLMES: Yes, and we may be doing entirely different things or meeting entirely different types of competition in our United States business than we are doing in our Canadian business. We don't do the thing exactly the same everywhere. You find out where you can do the best and you do that.

COMMISSIONER BROWN: You gather there is no difference in the intensity of this competition that is between a mutual company as such and a stock owned company.

COMMISSIONER GIBSON: Every once in a while in meeting that business you take a look at your affairs and say, "We have got to have something better and get it moving better again," and so on. What are the things that make you do this? Is it the fact that some other insurance company is getting ahead; is it possible that interest rates are going up or would a change in the banking rate --- in other words, what I am getting at is does your sales effort, your efforts on the liability side to get business, how does it respond to changes in environment, both competition with yourselves and other savings institutions and the general financial requirements?

think of these things all the time to find out if you are in difficulty -- if you have difficulties meeting their competition then there are certain areas where maybe you can do that, too.

COMMISSIONER GIBSON: It isn't just a question of the product. It is a question of how well you sell it.

MR. HOLMES: Yes, and we may be doing entirely different things or meeting entirely different types of competition in our United States business than we are doing in our Canadian business. We don't do the thing exactly the same everywhere. You find out where you can do the best and you do that.

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MR. RIEDER: I think in the agency department of all companies there is a continual drive for more and more business. Good quality business is considered, of course, but it is the automatic continuous selling regardless of everything else.

COMMISSIONER GIBSON: You would be in a position to offer more if interest rates were rising, would you not?

MR. RIEDER: Yes.

COMMISSIONER GIBSON: It might change your competitive terms?

MR. RIEDER: Rates might be changed under those circumstances but there would be still a continuous selling effort to increase the sales force in numbers and by volume sold per agent.

COMMISSIONER GIBSON: But suppose that money is tight and there is a certain amount of fear of inflation -- we have had these periods in the last two years -- does this bring forth an extra effort to help your position?

MR. BRYDEN: It brings forth an extra effort to help your field force; they are running into tough competition under thatkind of a situation and certainly you tend to put on as much extra effort as you can.

On this business of competition by the industry, possibly one of the examples here would be if you would look at the pension plans and the rapid increases in total assets. I am sure that is one of the major reasons which moved us into the position of

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asking last year for legislation for aggregate funds so that we also could have our group pension schemes at least partly invested in equities. During that period from 1955 through to, say, 1961, the number of pension plans which shifted over to some partial investment and complete investment in equities is very significant.

As a matter of fact, a lot of what we call insured plans shifted over to that type of investment. Now, that caused us to approach the Superintendent with a view to being able to establish these aggregate funds so that we could offer equity investment as a facility in our pension fund offerings. That will be an example of doing something on the over-all basis when you were losing out in relation to some other intermediates.

COMMISSIONER GIBSON: Extending your facilities to meet competition, and is this generally going on? Is this a trend in your opinion? You are widening the scope of your competitive activities?

MR. BRYDEN: I think to a considerable extent, yes. Certainly in that particular case it was, but I think that industry as a whole, since they do deal in guaranteed values, fixed dollar values, has been at somewhat of a disadvantage for the last 10 or 15 years because of the rather significant inflation which has gone on, where fixed dollars in X number of years from now were not as attractive as some piece of an equity that was supposed to double. That situation may be changing.

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COMMISSIONER GIBSON: But you don't think

that the insurance companies in their pressure to get business will respond very much to change in interest rates and tightness of money?

MR. BRYDEN: Not in their pressure to get business but that is the sort of thing that shows up in rate reductions, increased dividends, and so on. Your product under these conditions gets better but I don't think it changes one iota the pressure you are normally using through your field force to get business.

COMMISSIONER GIBSON: But are your rates and your competitive effort likely to change -- do they tend to change more rapidly now in the face of the increased competition for savings outside of your business than they used to be?

MR. BRYDEN: I would think the change in rates that is happening currently is much more a reflection of increased investment earnings and some extension of your mortality situation than it is necessarily competition from outside. Mr. Poyntz said earlier that they are going to try to do it as low as is feasible, and all this is part of this feasibility.

MR. POYNTZ: I think you are trying to get at how responsive are we to changes. Well, the company continually calculates its net yield, its interest return on various categories of assets and by different territories. It is continually investigating its mortality experience, and we are not using the old tables we are using the new modern tables tied to our own company's experience, and we are continually studying the expense factors and how they are applied to the various

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classes of business so that each year the company will determine whether it can make any changes in the premium rates for a particular plan or a group of plans or whether it can make any changes in dividend scale for existing business, and these do change from year to year.

Now, on the subject of short-term, because of changing premium rates and because they are going to oover long periods in the future, we can't respond immediately, we have to determine if we can how long this will last and what the average effect will be for the future lifetime of these policies, so we are limited in our reaction to it.

MR. BRYDEN: Mr. Chairman, on page 32, Section 3.57, we do state the example of one medium-sized company that since 1950 had reduced its whole life non-participating rates eight times, increased its dividend scale five times and changed its group pension rates 15 times to keep the price of its products in line with changing interest, mortality and expense experience.

COMMISSIONER BROWN: Do these changes all go in the same direction?

MR. BRYDEN: Yes, I would say so. You have reduced your rates at times and your dividends have been going up during that period, and as far as group is concerned I think that -- I don't know of any change that has been upward, I think they would all have been downward.

COMMISSIONER BROWN: I just wanted to get whether there was a trend they were following or whether

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they were jumping around.

MR. BRYDEN: No, that would be the trend.

MR. RAPSEY: I think there is one further point, Mr. Chairman, that hasn't been brought out, and I think if you look at the percentage change in this table 7a that it could be quite easily explained -- not easily explained, but there is one basis of reason.

COMMISSIONER BROWN: What page is that?

MR. RAPSEY: It is 7a on 118. To quote from a well known magazine published in the last few weeks it says that the best formula for investment by the modest capitalist is still a little money at the bank first, then you have coverage and then a good unit for mutual funds, so I think that explains it, that the mutual funds will grow more rapidly in a period of prosperity, if that thesis is acceptable.

COMMISSIONER BROWN: This brings back the supplementary question in an answer Mr. Holmes gave me in that the larger policy -- the people who under ordinary circumstances would be buying large policies of straight life, not only for investment but mutual fund ---

MR. HOLMES: You see, in the last 10 years there has been that tendency.

COMMISSIONER BROWN: Has this shown up in the average size of policy that has been written?

MR. HOLMES: They are large policies, they are term type policies.

COMMISSIONER BROWN: Has this shown up in the change in the average size of the ordinary life

policy?

MR. HOLMES: Well, the average ordinary life policy has been increasing quite rapidly through that period in size; what we have in this is a very definite lower cost type of policy, less saving element in the policy which is sold on the average and a lower degree of income per thousand of insurance.

THE CHAIRMAN: The insurance is more for the purpose of protection than as a method of saving?

MR. HOLMES: Yes.

THE CHAIRMAN: And when there is greater affluence people have more money they can put into savings and if they still want protection they can get it in that way?

MR. HOLMES: Yes.

COMMISSIONER BROWN: But the section on the question of legislation and supervision the suggestions you have made have all got to do with possible changes in the federal legislation; you have made no reference to possible changes in the provincial legislation and this may be because this is a federal commission and we are not interested in provincial legislation, but I was wondering if this was a fact and you are completely satisfied with provincial legislation.

MR. BRYDEN: I would like Mr. Tuck to reply to that.

MR. TUCK: In the area of legislation discussed in the brief most ---

COMMISSIONER BROWN: What page is that?

MR. TUCK: I was in the area of legislation

which is discussed in the brief.

MR. BRYDEN: I think it is page 37.

MR. TUCK: Which is legislation respecting investments and there are really only two provincial legislatures in which we have a substantial interest, and that is Ontario and Quebec because there are just two or three provincial companies incorporated in provinces other than those two.

Some years ago Ontario adopted the practice for its provincially incorporated companies of following the federal legislation after a lapse of a year or two. At the moment the investment powers of Ontario incorporated companies are the same as the investment powers of federal companies were prior to the 1961 amendment. These companies have asked for an amendment similar to the ones made by Parliament and the Superintendent and his Minister have approved of this and I think that the amendments were going to the legislature at the next session.

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In Quebec the situation is somewhat different. The investment legislation respecting the companies is not nearly as detailed as the Ottawa and Ontario legislation. In many respects it is more general; in one or two it is more confined. These companies have been considering whether to put forward suggestions. There may be some delay in reaction by the Quebec legislature because some years ago a commission was appointed to survey the whole field of insurance legislation and its report is in the government's hands and there has been no indication of the reaction. In those two provinces the companies concerned are just as interested in investment legislation as the government but because of the preponderant interest of the federal companies, and the fact that federal legislation also affects non-resident companies, the brief deals with it and makes short reference to the provincial picture.

COMMISSIONER BROWN: The provincial regulation in all provinces is the regulation of agency, isn't it?

MR. TUCK: Two big areas: The regulation of agents, agency practices and licensing of agents and the regulation of insurance contracts, and the companies have been very active particularly in the latter in proposing changes to the provincial superintendents of insurance, and within the last few days there has come into force in nine of the ten provinces a complete revision of the provincial law relating to life insurance contracts. This is uniform in all common law provinces.

COMMISSIONER BROWN: And you are all perfectly satisfied with the situation that exists with this

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MR. TUCK: Well, you are never perfectly satisfied. You put forward your proposals and you get some; you don't get them all. Actually, in the end the revision to the provincial laws reflects the views of the companies on a great many points, and we whole-heartedly supported the revision. We think it was a very substantial improvement over the old act.

COMMISSIONER BROWN: As far as federal supervision is concerned, I would like to fly a kite, and I don't want you to think this is other than flying a kite, but I would like to get some reactions. At the moment there is one individual who is Superintendent of Insurance; there is another one who is Inspector General of Banks, and there are other near bank institutions that come under, in large part, the Superintendent of Insurance. Are there disabilities connected with having a one man operation, or should it be, say, a three man operation supervising all financial institutions generally to get a correlation of policies?

MR. TUCK: I don't know that we have any answer to that. We think the federal supervision of our business has been constructive. We think it has been very efficiently handled and I don't think we have had experience in any jurisdiction where there is general supervision of all financial institutions. Problems are very different, but the fact the Superintendent of Insurance puts on his hat tomorrow and regulates small loan companies does not seem to be a disability

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as far as we are concerned. We don't know what he does in that area, but as far as we are concerned he and his staff devote a substantial portion of their time to our affairs and we think they do a first class job.

MR. HOLMES: I think those of us who have done business in foreign fields are very much impressed with the efficiency of the department at Ottawa and the insurance department at Ottawa.

MR. POYNTZ: I certainly agree with that.

COMMISSIONER LEMAN: In the solvency field do the provinces have the same kinds of tests? Are they as elaborate as the federal tests?

MR. TUCK: Yes sir, they are for the provincial companies. They have equivalent tests. Again, it is particularly Ontario and Quebec because that is where the companies are, and the record of the supervision has been quite good. No provincial life insurance company has lost money for its policyholders.

COMMISSIONER BROWN: On this question of legislation and supervision, let us deal with another general possibility: Would it be feasible to remove all controls over the types of investments you have?

MR. BRYDEN: It sounds like Mr. Brown is certainly starting to fly kites.

COMMISSIONER BROWN: Well, this exists in the United Kingdom?

MR.BRYDEN: It does pretty well exist in the United Kingdom. It could be feasible. It would present difficulties, I think, though as far as the Canadian companies that do business in the United States are

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concerned, they have a fairly tight set of rules and regulations over there. I don't know whether there is any United Kingdom company doing business in the United States -- is there?

MR. HOLMES: No.

MR. BRYDEN: It would be feasible, but I don't suspect it would be desirable. But as far as the rules and regulations are concerned under which we do operate, it seems to me that they are basically for the purpose of not allowing the companies into investments that have undue risk, or other regulations which tend to stop concentration of power, and within that framework I think we are all relatively free to do a fairly broad job.

COMMISSIONER GIBSON: If you were free of regulation, this would impede your business or handicap you in the United States, wouldn't it?

MR. BRYDEN: That would be my impression, yes.

MR. HOLMES: I would not think it would affect you if you stayed within the regulations in the United States but they would tend to regulate you then instead of the government here.

MR. BRYDEN: At the moment, on balance, they are prepared to accept the Canadian insurance laws. If these were non-existent, I think that in our operations in the United States we would then be made subject to the local state laws whatever they might be.

COMMISSIONER LEMAN: Does the regulatory body in the United States in the solvency field regulate

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COMMISSIONER LEMAN: Does the regulatory body in the United States in the solvency field regulate

you in the sense you have to report to them and they can test your solvency according to their own rules for the business you write in the States?

MR. TUCK: That is quite right, and each state has laws that require you to maintain assets in the United States to cover your liabilities there. I think Mr. Bryden is right in the sense that because of the existence of strong supervision in Canada the U.S. states don't concern themselves with the very important factor in relation to the protection of U.S. policy-holders, and that is, is the company as a whole solvent, because this is an extra protection over and above having trusteed assets in the jurisdiction. They might well say, if there was no Canadian supervision, "We must also put inspectors in to check on the solvency of the total company".

COMMISSIONER BROWN: Would this apply with the Canadian supervision of U.K. companies operated in Canada?

MR. TUCK: No. I think there are many factors there: The reputation of the U.K. companies themselves, and the ability they have shown over many decades to handle themselves properly has had the effect of the Canadian superintendent saying, "I can determine solvency of the total company by looking at their total statements, knowing that is filed with the Board of Trade, knowing that there is some general inspection of their total position there". I think that is the difference.

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[illegible]ISSIONER BROWN: Have you anything to

add, Mr. Westwater?

MR. WESTWATER: I don't think I have anything to add to that. We find some of the aspects of the legislation perhaps a little irksome as compared to the freedom we enjoy in the United Kingdom, but on the other hand I would say it is in some sense an advantage to us to be regulated, because it is an external company, and if there were any doubts shown with respect to the financial situation presented in Britain, the fact we have a strictly regulated position here is an advantage on our Canadian operation.

COMMISSIONER LEMAN: Coming back to the point made earlier, suppose you were successful in obtaining a system under which you would have subsidiaries for foreign operations separate from the main body doing business or writing business in Canada: Would that change the situation some?

MR. POYNTZ: I don't believe that would change the situation as far as our Canadian operations are concerned. I think we are considering the Canadian business, arn't we, and what has been said about regulation here, I think, would not be changed by that.

COMMISSIONER LEMAN: Are there not different characteristics in different countries about the yields you can get on various assets etc., so if you had one subsidiary writing business in the States, and one writing business in the United Kingdom, and another writing business in the Caribbean, then the solvency tests and the regulations etc., would be dovetailed to the particular area where it does business, and the

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parent body in Canada, writing business in Canada -- its rules, limitations, stringencies, etc., would be particularly adapted to the Canadian market. Wouldn't it be somewhat more flexible, or are the rules universal for testing insurance companies' operations -- should they be?

MR. POYNTZ: They are not universal. I think our reason for suggesting that there might be advantages to having separate companies by area is that we run into nationalistic regulations in certain areas rather difficult to comply with, and it would be perfectly obvious if we had subsidiaries these would only affect that small part of the company's business that was in the subsidiary.

We might explain that by relating to Cuba again: Some of the companies had Cuban investments covering their Cuban liabilities. The liabilities are liabilities of the whole company. The assets are affected by Cuban law and they may deteriorate for that reason, and yet the liability is not affected at all. The total company is assuming the liability. I think that is possibly one reason why we thought it might be advantageous in some way to segregate the whole business into one company in that area.

MR. HOLMES: I think I am right in saying we really haven't by any means made up our mind this is an advantage. I don't think any of us can think of any of these jurisdictions we would rather be supervised by than by the department at Ottawa.

COMMISSIONER BROWN: Would these jurisdictions

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MR. POYNTZ: They are not universal. I think our reason for suggesting that there might be advantages to having separate companies by area is that we run into nationalistic regulations in certain areas rather difficult to comply with, and it would be perfectly obvious if we had subsidiaries these would only affect that small part of the company's business that was in the subsidiary.

We might explain that by relating to Cuba again: Some of the companies had Cuban investments covering their Cuban liabilities. The liabilities are liabilities of the whole company. The assets are affected by Cuban law and they may deteriorate for that reason, and yet the liability is not affected at all. The total company is assuming the liability. I think that is possibly one reason why we thought it might be advantageous in some way to segregate the whole business into one company in that area.

MR. HOLMES: I think I am right in saying we really haven't by any means made up our mind this is an advantage. I don't think any of us can think of any of these jurisdictions we would rather be supervised by than by the department at Ottawa.

accept the Ottawa supervision?

MR. HOLMES: They don't accept it entirely, but they have accepted it remarkably well because it has a standing in the supervision field that is rather outstanding, I would say.

MR. RIEDER: I should not be talking on this topic because my company is confined to Canada, but to answer Mr. Leman's question, if a company operates in both Canada and the United States its United States business is subject to United States regulation and valuation laws and so on, even under the present system, for subsidiaries.

MR. HOLMES: As far as deposits in the United States are concerned.

MR. RIEDER: Yes.

COMMISSIONER LEMAN: How do they compare in general? Are they as tight as they are here?

MR. LEMMON: New York State is much tighter.

MR. TUCK: In general, Canada is half-way between the United Kingdom with little regulation and the United States with a whole lot.

COMMISSIONER MacKEEN: There are some regulations in some of the States ---

MR. TUCK: That was true of one large states for many years: It had a local investment law; that has been repealed.

COMMISSIONER MacKEEN: I see.

MR. TUCK: Whether there are any today -- I think there is one today which has a local law; the companies haven't gone into that state. However, they

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are in 48 of 50.

COMMISSIONER MACKINTOSH: I would like to bring Mr. Brown's kite down to earth and ask you if the investment limitations of the Investment Act were removed what difference it would make in the structure and management of investments?

MR. BRYDEN: If those investment regulations were removed I don't suspect it would make very much difference. We have now broad categories of assets within which we can invest. We also have the so-called 5 per cent basket which is open for non-authorized investments, if you will. My guess would be even if we did not have any investment restrictions that what we would do would not be significantly different from what we are doing now.

COMMISSIONER MACKINTOSH: Is this because you are conditioned to the law, or because you can't think of any more attractive investments?

MR. TUCK: The law keeps changing.

MR. LEMMON: I think the only area really where the law is restrictive, and where we feel it every day of the operation, is the 66-2/3 limitation on real estate mortgages, and that limitation is not removed by the basket. In other words, we cannot make a mortgage loan in excess of 66-2/3 per cent of the value of the property either in the basket or out of it. Whether the companies would, in fact, make 75 per cent or 85 per cent loans, or some higher percentage loans, if that was removed is a matter of opinion. I think there would be higher percentage loans made in some

areas, but I would think that is the only important area where restrictions of the Life Insurance Act really prevent us from doing something we might otherwise do.

COMMISSIONER BROWN: Let us look at the restrictions from a point of view of the percentage of various assets you can put in with regard to restrictions on solvency -- in other words, with mortgages you can only have 66-2/3 because that is the way they would be valued. In other words, are the percentages --- do you find them restrictive --the 5 per cent basket clause, the 10 per cent on real estate, the 15 per cent for common stocks -- you mentioned these others?

MR. LEMMON: You have mentioned the only really percentage limitation on us -- the 5 per cent basket and the 15 per cent in common stocks and the 10 per cent in income real estate.

COMMISSIONER BROWN: Yes.

MR. LEMMON: We did ask, as you will see in the brief, the Superintendent of Insurance to lift the 15 per cent restriction on common stocks. It is the opinion of the industry from the long-term point of view that should be lifted. On the other hand, with the exception of some of the long-term resident companies none of them are pressing on that at the moment. Nevertheless, the industry feels it should be raised. The 10 per cent limit on real estate is a fairly recent one. It was a percentage suggested by the industry at the time of the revision of the Act. I believe it is reasonably acceptable to the industry at the moment. Whether it will be always in future years, I don't know.

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The 5 per cent basket is also a new one lifted from three a year ago. The superintendent tossed back at the industry at that time that although very few companies used the basket up to that time, those few that had used it obviously wanted it raised, the others were not all that interested. I think some companies would still like to use five percent. I am not sure that that is industrywide.

COMMISSIONER BROWN: Then, let us move on to the measurement of the solvency which is also part of the whole picture, is it not?

MR. LEMMON: Yes.

COMMISSIONER BROWN: In other words, the basis on which your assets are valued for this solvency reserve fund.

MR. LEMMON: Yes.

COMMISSIONER BROWN: In that the only point which has been taken up in your brief is the question of using the amortized value for the measurement of municipal securities and I gather there has been a minority of reports that is not fully in favour of such change because of the inefficiency of trading operations.

Now, to what extent do the use of amortized values on federal and municipal governments and their securities inhibit trading?

MR. LEMMON: Well, Mr. Chairman, if I might, this is a matter of discussion within the industry itself. When we asked for the extension of the amortized principal to other types of bonds, namely,

municipals, as you are aware there was a minority view of this industry felt quite strongly that it does. Certain companies felt that it does not.

You understand the background of that, of course, that if you have a bond where you can claim for valuation purposes par for a 3 per cent, say, and that 3 per cent bond is selling at 85 in the market and you sell it you lose in fact the protection of that value for annual statement purposes.

There is a feeling there would be a disinclination to sell that bond even though it might be a desirable sale rather than lose that protection of par value for statement purposes rather than current market. Some of the rest of us feel that it is no more deterrent, the amortized value is no more a deterrent than the book value. I do not think the industry could present a united front on that one. Some of us feel it is not a major deterrent to trading and other members of the industry feel that it is. We have not any statistics to prove it one way or the other.

COMMISSIONER BROWN: How real are these measurements of solvency in a market like the present when you have got an amortized basis of valuation as such a large proportion of your whole investment?

MR. LEMMON: Well, you realize, of course, Mr. Chairman, that in the United States they permit the use of amortized values. Not only do they permit the use of amortized values, but they require the use

of amortized values for your statements at the end of the year on the theory that as long as the bond remains in good standing and there is no doubt whatever about the payment of interest or sinking funds or principal at maturity then why should a life insurance company's assets fluctuate in value due to changes in interest rates and bond prices change in value on the market?

Bond prices change in value on the market for two reasons. One is a change in the basic interest rate structure and the other is some change in the credit rating of the borrower itself. We are not dismissing the latter really because the United States by use of ratings for securities attempts to eliminate those from the amortized list. So when you are only talking about those bonds about which there is no question about the type of interest or interest rate or principal, the philosophy is that a life insurance company in a long term transaction, not being subject to the presentation of liabilities on demand as a chartered bank is, for instance, could afford to purchase bonds and hold them through to maturity on the yield on which they were purchased, and get this money in accordance with the contract and not really be concerned with fluctuations during it.

It is the feeling of a number of the members of theindustry that to value life insurance companies' assets or particularly the security section of them on market values at the end of the year is to put the life insurance companies on an arbitrary basis as of a

given date which is not the realistic value of the nature of a life insurance company's operation.

COMMISSIONER BROWN: I gather from the brief that the external companies operating in Canada have their assets valued on a market value basis.

MR. LEMMON: That is right.

COMMISSIONER BROWN: Why are the different restrictions imposed?

MR. LEMMON: I could suggest that that question be levied at the superintendent of insurance because he is the one who lays down the regulations, but fundamentally I believe -- and again perhaps I am putting words in his mouth that might better come directly from him -- that he has not control over the total operations of those companies but only over one little segment of them and they may well be put on a liquidating basis at any date. In other words, if a company organized under the laws of Timbuctoo came in to do life insurance business in Canada and then decided some years later they did not want to do life insurance business in Canada any more, you might find it very difficult to pursue them to Timbuctoo and be on the basis of reinsuring the liabilities with some other companies in Canada and he might probably in that case get it best on the market value of the securities deposited. That is not the way of purchasing the obligations of a purely Canadian company. Are you clear on that?

COMMISSIONER BROWN: Yes.

MR. TUCK: There is no statutory requirement

for an insurance company to maintain any surplus in Canada comparable to the surpluses that Canadian companies do in fact have. If there was such a requirement for a surplus of 6 per cent, 8 per cent, 10 per cent, the superintendent might look differently at the market value point which Mr. Lemmon has discussed.

COMMISSIONER BROWN: As a point of information this computation of market value for the external companies, does this result in assets being written up, as well as being written down? Is it below the cost of market or market?

MR. TUCK: Year end market.

COMMISSIONER BROWN: In other words, the common shares that are given out?

MR. LEMMON: As the market goes up and down.

MR. BRYDEN: You, Mr. Westwater, do not write up or down your particular securities. These market values come off at the valuation for solvency purposes. You do not internally write them up.

MR. WESTWATER: No, for the purposes of a solvency review we are required to use market value and appreciation in common stocks may mean, of course, that the 15 per cent limit has been exceeded and we have then not been adding stocks to our portfolio in which event we are obliged to restrict our purchasing activities until that situation is corrected or until we put out some other form of guarantee. That is one of our complaints, as I say, against the existing regulations on market value.

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COMMISSIONER BROWN: On the Canadian market valuation can you clarify one point for us? Each individual security is valued at the lower of book or market?

MR. LEMMON: There are two columns in our annual report ---

COMMISSIONER BROWN: I am leaving out the ones that have to be done on an amortized basis, the ones that have to be done on a market.

MR. LEMMON: I am not sure what you mean. In our return to the superintendent of insurance at Ottawa there are four columns, the par value, book value, amortized value and market value -- four different columns and your total is the sum of amortized values, book values, market values, and this is the total values that he permits for statement purposes. We do not change the book values year by year.

COMMISSIONER GIBSON: In your statements?

MR. LEMMON: In our statements.

COMMISSIONER GIBSON: You do not change them?

MR. LEMMON: We do not.

COMMISSIONER GIBSON: In other words, if the market goes up you do not mark your stock up?

MR. LEMMON: No.

COMMISSIONER BROWN: You did mention that he looks at the aggregate total, not individual securities?

MR. POYNTZ: But he does not add it in your insurance.

MR. LEMMON: Amortized to par at maturity. In certain cases companies have written down the book

value of securities purchased for reasons best known to themselves below their original cost. That may be an arbitrary write down or it may be because they think the security is impaired. They do not have to carry it at the amortized cost in their books.

MR. BRYDEN: If the aggregate total is greater than the book values then the book values are retained and if, alternately, the aggregate total is less than the book value then there has to be some provision made on the liability side of your balance sheet to carry it usually doing it by setting aside some part of your surplus account for that purpose.

COMMISSIONER GIBSON: Equal to the rate that is down on your asset side.

MR. BRYDEN: As a result you might write some down. You could write those down and might be suffering some distortion or something of that kind but in normal practice it is just your book values for that purpose.

COMMISSIONER GIBSON: Supposing you have a certain stock on your books which you have purchased at a price which is much below current market value, let us say purchased at 30 and is now selling for 60. Then you bought some more at 80 and it goes down to 60, do you have the one account of all the stock and treat it as one item or are there two separate accounts?

MR. BRYDEN: I think most companies take an average book price of stock of that kind.

COMMISSIONER GIBSON: If it is the same as what you already have you would take an average book

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COMMISSIONER GIBSON: If it is the same as what you already have you would take an average book

value?

MR. BRYDEN: Yes.

COMMISSIONER GIBSON: And providing the average book value was below the average market value it would stay that way.

MR. BRYDEN: Yes.

THE CHAIRMAN: We will now adjourn until a quarter to two.

(At 12.10 P.M. the hearing adjourned until 1.45 P.M.)

On resuming at 1.45 P.M.

THE CHAIRMAN: We will now resume, gentlemen.

COMMISSIONER GIBSON: Mr. Chairman, there are one or two questions relating to our discussion this morning that we overlooked asking about. I want to ask them now in any case. One qestion I meant to ask but did not had to do with the commission system for insurance agents as against the salary system. I gather that both systems are used to some degree; most companies use mainly the commission system but one or two use a salary system. Do you care to make any comment about the effectiveness and usefulness of the two ways of selling insurance?

MR. BRYDEN: Mr. Chairman, I must confess that I am not too aware of the companies that use a salary system as such.

Most agents are under contract which is based on a percentage of the first premium, a smaller percentage of the second and then another still smaller commission for about the next 8 years. I would have thought that the predominent method of remuneration in the insurance sales business, although I know that all companies have assorted methods of weighting and so on in respect to these contracts to produce what they hope will be the best results.

As far as the straight salary contract is concerned, I am not particularly aware of that.

MR. POYNTZ: Mr. Gibson might be referring to what some companies use during the early stages of a salesman's career.

COMMISSIONER GIBSON: No, sir, I was told that one of the British companies was using a salary system.

MR. WESTWATER: We have a mixed system. Perhaps I should describe it as a basic salary which is related to different quotas on volume of production expected from the man, and we bonus him on volume over that at the end of the year. In addition we pay a small commission on each sale, so it is really a mixed system. The salary gives him basic security and we find that it appeals to us. We think we have a higher quality of man which we can attract in the first place with this salary security behind the contract. Without the commission on the sale or the bonus on the total volume it would lack the necessary incentive to the insurance salesman.

COMMISSIONER GIBSON: It still is basically an incentive system with a minimum salary arrangement?

MR. WESTWATER: That is right. It is not so very different from the drawing account system I think that some of the companies operate in respect to salaries. It is a contractual amount of money.

MR.HOLMES: That is in respect to the ordinary business, but yours is somewhat a specialized business.

MR. WESTWATER: That is what I was referring to: The ordinary business.

MR. HOLMES: In the ordinary business you have very little control of a man's time and it seems essential that you have a system from which you will get results, unless you use a salary system and cut them

[illegible]

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right off when they fail to maintain a quota, which is practically a commission system anyway. If you cut them off when they fail to make their quota you have practically a commission system.

COMMISSIONER GIBSON: But as it stands now some of the Canadian companies do pay sort of a minimum amount during the learning period, is that correct?

MR. POYNTZ: That is right.

COMMISSIONER GIBSON: And you have no particular comment you want to make about this system of selling insurance? You are quite satisfied with it?

MR. BRYDEN: I should think it was the most effective method of gaining the full attention and effort of the field staff because certainly their income depends on their degree ofsuccess. In early years, or in cases of new agents, what one normally does is set up in effect a salary. It is an advance at a certain level and it continues for a certain time based on the production performance, so that you give a certain limit of time and if the production is not meeting the requirements then the chances are that the man is not going to be successful and the contract is terminated.

COMMISSIONER GIBSON: Has the cost of selling insurance per dollar of insurance been increasing or decreasing, or what over the years? Have you any figures in that regard?

MR. HOLMES: I think over a long period there has not been a great deal of change. Since the war there has been quite an increase but that was due to a decrease during the war period, I think. I doubt if there has

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been a great deal of change over all in the cost of actually selling insurance from early days.

MR. POYNTZ: Mr. Chairman, in regard to the system of agency operation, which is really a Canadian system -- incentive system-- some information appears in paragraph 3.20 at page 22 of the submission. In 1960 Canadians held life insurance in an amount 2.2 times their total wages, salaries and the earnings of the self-employed. The corresponding ratio in the United States is 1.7, and in other countries it is lower than that. The British ratio is lower than 1.7, and it is in that country that there may be more sales on a salary basis than anywhere else.

COMMISSIONER BROWN: Have you got comparative costs per $1,000 life insurance sales for the different companies?

MR. POYNTZ: No, I am sorry.

COMMISSIONER BROWN: Does it cost more to sell $1,000 worth of life insurance in Canada than in the United States?

MR. POYNTZ: I would say no, but I have not any figures in that regard Mr. Brown.

COMMISSIONER BROWN: You did mention that possibly this was the more effective way of doing it.

MR. POYNTZ: Yes.

COMMISSIONER BROWN: Is it a more expensive way of doing it?

MR. POYNTZ: It is possible, yes. It is not very different from the United States system. It is different from the British system and some of the

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European countries where the ratio is much lower than even the 1.7 in the United States. I have not got figures on the sales.

COMMISSIONER BROWN: Another point that arose out of this discussion, and this is probably even more difficult to get at; life insurance is a very effective way of mobilizing savings, but is it an expensive way of accumulating savings? Have you any idea what the cost is of accumulating life insurance savings? Your 25 per cent of total savings would take place, but is the cost of accumulating these savings successful?

MR. HOLMES: I think of the people we get to save it is not an expensive way of accumulating savings. I think anybody else who sells savings to the same type of people on a regular basis like we do would have to pay higher costs. You find that in mutual funds. They pay very similar costs in selling as the life insurance companies do. But, in so far as natural savers it is a fairly expensive system. It is much cheaper to put the savings in the bank.

COMMISSIONER BROWN: I suppose credit unions accumulate savings cheaper?

MR. HOLMES: Credit unions accumulate savings cheaper, but their overhead on savings is provided through the staffs of recognized companies. It is not a professional job to the same extent. It is a co-operative sort of job which has a certain appeal to people who give their time. The accountant gives the space and there is a certain amount of other work done without a great deal

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of expense. It is the natural savers who save but we reach out a little further than that.

MR. POYNTZ: It is probably fair to say that if we did not have this kind of agency system, which is a fairly attractive incentive plan for salesmen, we would not really be a factor in the savings stream at all.

COMMISSIONER BROWN: I think we agree, as I say, that it is a very effective way of saving. I was trying to figure out if there was any measure of how expensive a way to save it is.

COMMISSIONER GIBSON: In Great Britain Canadian companies compete with the British companies. Do they do this fairly effectively?

MR. POYNTZ: Yes, fairly effectively.

COMMISSIONER GIBSON: They have added quite a lot to their business?

MR. POYNTZ: Yes, Canadian companies have done well in Britain but I think probably the reason is that they have taken a kind of agency system there and it is that which has done this rather than a comparison of costs.

COMMISSIONER GIBSON: Are you selling much the same article?

MR. POYNTZ: Much the same. I would think the British sell more annuities than the Canadian companies do, but generally speaking, much the same.

MR. BRYDEN: Mr. Gibson, this may throw some light on the question you are asking. The life insurance fact book in the United States takes the

[illegible]

MR. POYNTZ: It is probably fair to say that if we did not have this kind of agency system, which is a fairly attractive incentive plan for salesmen, we would not really be a factor in the savings stream at all.

COMMISSIONER BROWN: I think we agree, as I say, that it is a very effective way of saving. I was trying to figure out if there was any measure of how expensive a way to save it is.

COMMISSIONER GIBSON: In Great Britain Canadian companies compete with the British companies. Do they do this fairly effectively?

MR. POYNTZ: Yes, fairly effectively.

COMMISSIONER GIBSON: They have added quite a lot to their business?

MR. POYNTZ: Yes, Canadian companies have done well in Britain but I think probably the reason is that they have taken a kind of agency system there and it is that which has done this rather than a comparison of costs.

COMMISSIONER GIBSON: Are you selling much the same article?

MR. POYNTZ: Much the same. I would think the British sell more annuities than the Canadian companies do, but generally speaking, much the same.

MR. BRYDEN: Mr. Gibson, this may throw some light on the question you are asking. The life

[illegible]

life insurance company dollar in 1960 and breaks it down as to source and disposal. In 1960 in the United States among the operating expenses, commissions to agents are listed as 7.5 cents. We have tried to reproduce the same thing in Canada. In the Canadian fact book again in 1960 the commission agents are listed at 5.5 per cent. On that basis one would assume that our actual commission costs are less than they are in the United States.

COMMISSIONER GIBSON: This is the percentage of the dollar -- ?

MR. RIEDER: This is the percentage of the premiums plus the net investment income, to give you your dollar, and the outgo is broken down, and of the total income the commission's two agents in the United States were 7.5 and here, 5.5 cents.

THE CHAIRMAN: $5\frac{1}{2}$ cents in Canada?

MR. BRYDEN: Yes.

COMMISSIONER BROWN: One other question; you mention in your sales force that you had a large turnover. I assume all of the companies are now using apptitude tests and this sort of thing?

MR. BRYDEN: Yes.

COMMISSIONER BROWN: In trying to pick out those who are worthy of training as salesmen you use these tests. Has this been effective in reducing your costs of acquiring an efficient salesman?

MR. BRYDEN: Well, we would like to think that it had; just how effective it has been is open to question. Certainly you take on a lot of new

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MR. BRYDEN: Well, we would like to think that it had; just how effective it has been is open to question. Certainly you take on a lot of new

representatives over the years and there is a large number of them, despite all the aptitude tests and everything else, that turn out not to be able, if you will, to just merchandise money for future delivery. There is a large number that disappear out of your work force after the first, one, two or three years. Usually once they last that long the rest of them pretty well have a rather long-term career.

COMMISSIONER BROWN: Is that experience pretty general among all companies; the same percentage?

MR. BRYDEN: I think that is one of the biggest problems in the agency end of the business; Selection of personnel and keeping them. On the other hand, I do not think the turnover in your agency force is any greater than it turns out to be in your administrative staff where again you have a considerable number leaving you after a relatively short work period, although the reasons for it are a little different. I would think that is a fair example of what seems to go on.

MR. POYNTZ: We have been concerned about turnover of our agency force but in comparing it with sales forces in other businesses, that turnover is not relatively greater.

COMMISSIONER BROWN: Do you think they are getting your discards and you are getting theirs?

MR. POYNTZ: I hope not.

MR. BRYDEN: I should try not to.

MR. POYNTZ: I think one of the results of selection and aptitude is that the survivors of the first two or three years are better trained and qualified

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MR. POYNTZ: I think one of the results of selection and aptitude is that the survivors of the [illegible]

now than they were some years ago, but it has not actually had much effect on the early turnover.

MR. BRYDEN: I think the big advantage of the aptitude tests and the rest of those things is that they at least screen out those that are sure to be failures. It certainly does not catch all of them, but I think it is very helpful in administering the field force.

COMMISSIONER GIBSON: Do you get many trained people who have specialized training like law and accounting going into the sales field these days?

MR. BRYDEN: I would say not too many from our experience.

COMMISSIONER GIBSON: There are more of these people now around than there used to be?

MR. POYNTZ: That is rather rare I would think, Mr. Gibson.

MR. HOLMES: I think that perhaps in law there are more today than there were a number of years ago, but we have a certain number of trained men in certain agencies where you have a very high calibre of selection and training. We certainly have quite a large number more than before.

MR. BRYDEN: Of course you require a fairly high degree of competency when you get into business insurance and estate administration and that sort of thing.

COMMISSIONR GIBDON: That is what I had in mind.

MR. BRYDEN: So you have a fair sample of people right across. Some are in that tight market and

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MR. BRYDEN: So you have a fair sample of people right across. Some are in that tight market and

some are in the other markets.

COMMISSIONER BROWN: There is one other field we discussed briefly this morning that I should just like to re-open, and this has reference to the problem of one company taking over another company, or amalgamating. Now, the Act as it stands, as I understand it, prohibits a company from buying the shares of another company. The question I did not ask directly this morning and should like to now ask is whether under the Act there is any prohibition against one company offering additional treasury stock for shares in the other company, and if there is -- well, I will ask the first question.

MR. BRYDEN: I do not think that is covered in any prohibition in the Act. It would certainly be covered under the limitation of not more than 30 per cent of the capitalization of any one company, so that I do not think you could effectively do what you suggest under the present Act. Mr. Tuck, have you any information on that?

MR. TUCK: I do not see any reference in the Act to a bar of the type you suggest, but there are some companies with authorized capital only partly issued. There are only very few instances of treasury stock being issued. I think that Mr. Bryden has covered the point although I am not sure that I understood the question in relation to the30 per cent rule.

COMMISSIONER BROWN: I did not mention the 30 per cent rule.

MR. BRYDEN: No, I mentioned that.

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COMMISSIONER BROWN: I did not mention the 30 per cent rule.

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MR. TUCK: Mr. Bryden mentioned that rule.

MR. BRYDEN: My point was that even if you did have a treasury stock issue and were able to acquire 100 per cent of the stock of another life company I think you would then be stopped by the prohibition that you cannot own more than 30 per cent of the shares of any other company. So, it would seem to me that would be the prohibition in respect to an attempt to do what you have suggested.

COMMISSIONER BROWN: What I was getting at was another way of bringing about an amalgamation.

MR. BRYDEN: I would think you would be caught on that rule.

COMMISSIONER BROWN: Has it ever been tried?

MR. HOLMES: You could re-insure the whole company with the approval of the treasury board and in that way take over the whole company.

COMMISSIONER BROWN: In other words you could buy the assets of another company?

MR. BRYDEN: And the liabilities.

MR. HOLMES: If it goes through both companies, the shareholders and policyholders and goes to the treasury board and it gets their approval. There has always been that method of taking over a company.

COMMISSIONER BROWN: Has this been done?

MR. HOLMES: Oh, yes it has been done.

MR. TUCK: Not in recent years except for the one instance that was mentioned this morning. In the last year or two two of the smaller companies amalgamated, but that is the only instance for 30 years,

I believe.

MR. POYNTZ: I would say that is right.

COMMISSIONER BROWN: Following on this, the question or point was brought out that there was an apparent policy against this acquisition because it would reduce competition in Canada. When an American company buys out a Canadian company and that American company is already operating in Canada on its own, does this not create the same situation; there is a reduction in the number of companies in the market? Let us use company names. When Aetna bought out Excelsior, did one of them cease operating in Canada?

MR. TUCK: Aetna is going to cease doing new business in Canada, but I think that is the only instance, sir. In other cases the non-resident life company that has acquired control of the Canadian company has not been doing life business in Canada.

COMMISSIONER BROWN: Then this recent example would appear to be against the policy that was enunciated by the superintendent in his 1959 report to which reference was made earlier?

MR. POYNTZ: I think that is true because it did take the United States company out of the Canadian market and put all their business in the acquired Canadian company.

MR. HOLMES: There was no prohibition of the United States company buying the Canadian company's stock. They did not buy the whole of the Excelsior stock.

COMMISSIONER BROWN: They just bought control.

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COMMISSIONER GIBSON: How relevant is this to the idea that a number of companies should not be reduced? Have they been increasing substantially in the last 15 or 20 years? Is there a fairly hard degree of competition? I gather from what you say there is.

MR. POYNTZ: Very hard.

COMMISSIONER GIBSON: There is no individual company or three or four companies doing all the business?

MR.POYNTZ: No.

COMMISSIONER GIBSON: Do you think this concept is a particularly relevantone?

MR. POYNTZ: I do not think it is, Mr. Gibson, with the large number of companies now operating.

MR. RIEDER: It has reference to the number of Canadian companies that are now Canadian controlled. I am not sure how many there are.

MR. POYNTZ: There are 58, 36 of which are federally registered and 22 provincially registered, as well as 63 non-resident companies operating in Canada.

MR. HOLMES: This concept goes back a long way. There was a time in 1917 when the Sun Life went through all the necessary requirements of re-insuring the Manufacturers Life. We have gone through the requirements but Mr. Finlayson vetoed it.

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one against the other.

One other point that was brought up this morning but was not pursued was of interest to me. Mr. Brown asked you if you thought of any different system of regulation. That is, just having a board rather than a single superintendent in your particular area. Possibly such a board might regulate a wider area of the financial system and inspection system. You told us that you thought well of the present system. Do you see any objection to a board as opposed to this system; such as a three-man board to include the banking system as well as the insurance system?

MR. BRYDEN: Mr. Gibson, are not most of these separate financial intermediaries specialized occupations?

COMMISSIONER GIBSON: I think they are.

MR. BRYDEN: Certainly the insurance business is and our present Superintendent of Insurance is a very able man, and his staff is very able. I would suspect that the Inspector General of Banks has a completely different set of facts and figures to deal with. Whether all of it could be successfully put under one board which would handle the whole thing, or not, I would very much doubt. My suspicion is that the present method is preferable.

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some expansion in this area. I merely ask you for your thoughts, not expressing an opinion at all.

MR. BRYDEN: I do not think we are expressing any opinion either other than the present system seems to work extremely well.

COMMISSIONER GIBSON: You do not see anything fundamentally wrong with this idea of a board that might cover most of the financial system?

MR. BRYDEN: I do not think you could say it was fundamentally wrong. Again all I can reiterate is that the present system seems to function very well.

COMMISSIONER GIBSON: Emphasizing the point that you would want to have a man that really knew the business in charge of that paticular kind of business?

MR. BRYDEN: That is right.

MR. RIEDER: One member of the board would have to specialize in our field.

COMMISSIONER GIBSON: So that if you had a board you would have probably each of the members being an expert in respect to certain parts of the financial business?

MR. BRYDEN: The present Superintendent I gather has the rank of a deputy minister in the Department of Finance, so that your reference is at a reasonably high level.

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COMMISSIONER BROWN: Referring to one other thing which was touched on this morning, you were talking about the present regulations with respect to valuation of securities and I think there was mention of a 66-2/3 per cent restriction on the markets.

Have you any comments on any of the other qualifications; for instance, the five years Dominion requirement for preferred shares or the seven years Dominion requirement for common shares.

MR. LEMMON: I think not, Mr.Chairman. This received very thorough discussion within the industry at the time of the last revision of the Insurance Act. There are certain limitations on that as a test we can realize, but that taken in conjunction with the fact we are allowed to invest 5 per cent of our efforts free of these restrictions seems to be a workable test; a five year test on prepared and seven years on common, and the earnings test for various types of debentures and that sort of thing have evolved over the years, and they are easily administered and easily understood and seem to be workable restrictions that have meaning.

COMMISSIONER BROWN: On the same question I did want to find out what you thought about the removing of restrictions from percentages and the qualifications for investments. How about the qualification that in the sense that these restrictions will apply only to your legal requirements and your surplus was free of all restriction?

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that situation at the moment with the 5 per cent basket, and generally speaking the surpluses to the Canadian life companies are in the area of 6 or 7 per cent of assets, and we are not very far off that position at the moment.

COMMISSIONER LEMAN: What has been your experience over a period of years on the yield of basket assets; how does it compare with the yield of regular assets?

MR. BRYDEN: I do not know whether any of the companies have filled out a separate yield on their basket investments. We have all sorts of breakdowns on the total assets in various sections of it, but I do not think -- at least, we have not filled out a separate yield on these particular securities that were involved in the basket. My guess would be that it probably is not too far from your normal situation and it probably is occasioned for different reasons. One reason is that you may include in your basket some securities on which the yield is relatively low and yet which may have a capital gain in sight. On the other hand, you may put into your basket some types of real estate, for example, where the yield is probably higher than normal and my suspicion would be that you are probably not far from the average. Would you agree?

MR. POYNTZ: I would think so.

MR. HOLMES: Thinking of ourselves, I would say that we have had some of those kinds.

COMMISSIONER LEMAN: Would you say that in general life companies would be looking for -- you use

the basket clause mostly for capital depreciation.

MR. BRYDEN: No. No, you use it quite often in situations which are not quite legal yet; in other words, the common stock that you may think highly of.

MR. HOLMES: There are quite a number of people who bought uranium bonds and they turned out to be a very good investment, but they were not to be dealt with other than by the basket.

THE CHAIRMAN: What about leasebacks?

MR. HOLMES: They do not need to be in the basket, but real estate other than leasebacks would have to be in the basket.

MR. BRYDEN: The leasebacks themselves get about 10 per cent relative to real estate.

COMMISSIONER BROWN: On this question of the common stock where you suggest increases of 15 and 25 per cent, there are a few things I would like to get on the record. The first is what is the essentially different philosophy of the British companies that have larger percentages than the Canadian companies. Why do they go into common stocks?

MR. BRYDEN: Perhaps Mr. Westwater would like to answer that.

MR. WESTWATER: The philosophy is associated with the nature of our business in long term fixed liabilities and to realize this, with the maximum good to our policyholders, we must achieve the maximum yield. We believe that the common stocks would, in the long run and with a reasonably prosperous economy, in the

long run they will show a better yield probably than any other class of investment. That has been our experience in the United Kingdom and we are prepared to take a chance on that in a country like Canada, too.

MR. BRYDEN: Would you care, Mr. Westwater, to comment on the evaluation problem in the U.K. that allows you to take that position.

MR. WESTWATER: Of course, that is rather the reason why the domestic -- Canadian companies do not invest in common stock. British companies have no restrictions on their evaluation basis and the companies select whatever rate of interest, mortality, and so on that they wish, and it is a valuation of the liabilities. If for any reason the value of assets is depressed, then he is free to relax his standards and he is not embarrassed. He does not then have to show a technically insolvent position. There is rigidity in the Canadian system because of the regulations by the government and this is significantly inherent in the contracts which Canadian companies issue on cash values. Canadian cash values are linked, I think in most cases, to reserve values and in Britain a great many companies can guarantee cash values but not all go so far as that and none link them in a contractual way with reserves.

COMMISSIONER BROWN: Presumably you must operate within certain limits. You cannot suddenly decide to put this on an 8 per cent basis.

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COMMISSIONER BROWN: So there are certain limitations?

MR. WESTWATER: Limitations of practicality.

COMMISSIONER BROWN: It does give flexibility for the market structure.

MR. WESTWATER: Yes.

COMMISSIONER BROWN: If interest rates force down values the use of liability is on the same basis?

MR. WESTWATER: That is right.

MR. BRYDEN: A lot of them we have tried to set forth in fair detail on page 84, section 5.75, from there on, and we have attempted to explain the differences in the two countries.

COMMISSIONER BROWN: When we finished before the luncheon adjournment we were discussing this question of the valuation at the end of the year and we have the four columns; the par value, the book value, the amortized value and the market value. I would just like to get straight the rigidities, if any, that come into the investments that are related to market value and ignore the amortized ones at the moment.

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that affect whether the surplus has to be touched or not. Now, if we take a hypothetical example that may come out the same, then there is no adjustment to surplus at the end of the year, but, of course, within the range that there will be some that will be written at book value and others below book value. Now, if you sell, say, in February or January something at the market value which is below the other value, how do you adjust for this; do you adjust for this by writing off against surplus the actual production against surplus, or have you power to write off some other assets?

MR. LEMMON: No, it is charged against surplus; a realized loss charged against surplus in that year.

COMMISSIONER GIBSON: The profit would be the same; you would have to add it to the surplus?

MR. LEMMON: No, you may use that profit to cut down the value of the same security in your books.

COMMISSIONER GIBSON: So, you are taking the last realized profit and at the same time cancelling one as against the other, but it would have to be realized?

MR. LEMMON: Yes, that is right.

COMMISSIONER BROWN: This perhaps was one of the points you were making earlier?

MR. LEMMON: Yes.

COMMISSIONER BROWN: That the rigidity in the section that is based on mortgage values is somewhat

similar to the rigidity in the section based on amortizing.

MR. LEMMON: Yes.

COMMISSIONER BROWN: And you mentioned that some companies do not regard this rigidity as very important; you are prepared to take it if there could be shown a reasonable opportunity for improving the situation that there are other companies, presumably, that do not look at it in the same way.

MR. LEMMON: It is a matter of degree.

COMMISSIONER BROWN: Could we hear some opinions from some of the others on this?

MR. BRYDEN: Possibly Mr. Rapsey could speak to this.

COMMISSIONER BROWN: I do not want to get you quarrelling.

MR. HOLMES: We are in a company that really does not like amortized values at all. We have been prepared to go along with them up to a point, because we feel it definitely brings in rigidity, but we really prefer that old system where we admit at times your market values become impossible for the buyers, but we had a system where the Superintendent took cognizance of that and gave special values during periods of that kind. At least you are faced with the situation as it stood and we feel that there has been a great advantage to our particular company to not have to worry about whether you were thinking of the thing being worth the market value and you had no losses on your books of sale. If you had to think of it as a market value

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there was no loss on your books, and if it is allowed there we feel it would make a very considerable addition to our income because we do not have to worry about whether there is a loss or a profit and we looked on it that the value of that security was the market value and we would be very much adverse to having the thing made more rigid, such as is done in the United States.

COMMISSIONER BROWN: Why is there this reluctance to take this loss?

MR. BRYDEN: I would say the answer to that is that, from a balance sheet point of view at the end of any particular year if you had a substantial increase in the interest rate with a corresponding decrease in bond values, there is a limit to the extent to which you want to throw up the realized losses within a given year, and I suppose the answer to that is for fear that it may be misinterpreted when your statements come out because it certainly is offset against your surplus.

Now, in the throws of a major move of that kind, if you wanted to move a substantial volume of your assets on a trading basis the net loss could be quite substantial.

COMMISSIONER BROWN: It is really an accounting rigidity?

MR. BRYDEN: Yes.

COMMISSIONER BROWN: Because it does not change the actual situation at all?

MR. BRYDEN: No, it is an accounting rigidity.

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MR. BRYDEN: Yes.

COMMISSIONER BROWN: Because it does not change the actual situation at all?

MR. BRYDEN: No, it is an accounting [illegible]

COMMISSIONER BROWN: What we are trying to get at is to what extent this Canadian rigidity effects the development of the capital market.

MR. BRYDEN: It has a restraining influence on the trading in a number of cases.

COMMISSIONER BROWN: How important is this situation? Is this your own estimation of the importance of it? Do policyholders look at it?

MR. HOLMES: I think it would be pointed out to them -- if they did not look at it themselves -- by our competitors.

COMMISSIONER BROWN: But the answer is ---

MR.HOLMES: If one company has a normal increase in surplus and another company shows a reduction in surplus in the year, it would certainly be pointed out.

COMMISSIONER BROWN: Even if the actual situation was the same?

MR. HOLMES: Oh yes, because it is a very complicated business, knowing what the actual situation is, or it is a very simple business where a statement is seen where there is a loss in surplus. It is the same with such people as your Board of Directors. If you are looking at the thing from a rigid viewpoint and showing heavy losses on sales you would have difficulty getting them to agree to deal with securities freely, whereas if you get them educated to thinking that market value is the proper basis, you do not have that difficulty.

COMMISSIONER BROWN: Fifteen companies have gone through the process in the last few years and it

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COMMISSIONER BROWN: Fifteen companies have gone through the process in the last few years and it

has affected their services through mutualization. Is that the answer to this, something that can be explained to the public? This apparently has not inhibited you in making this move.

MR. HOLMES: I do not think any of them have to show a list of surpluses in the process. For one reason or another they produce money from somewhere.

COMMISSIONER GIBSON: Mr. Holmes, you were saying you would not like to see this -- are you not inhibited by this system? There was a hypothetical example given and Mr. Brown raised the question where your book value and your market values are the same that some of the securities are under the market and some are over the market; you sell some of the securities when the market is under and you have to deduct that from your surplus, do you not, that loss? That must inhibit you to some extent like everybody else?

MR. HOLMES: Not if you report to your board consistantly on their market value positions and selling at a loss on your book value does not affect your market value position, the value at the market.

COMMISSIONER GIBSON: But it still does affect your surplus or might affect it?

MR. HOLMES: It might affect your surplus, yes, but we have not been embarrassed by that, and we have been able to, as I say, to yield securities in a very substantial way.

COMMISSIONER GIBSON: And you operated purely in relation to market forces? You have not let this particular thing concern you?

MR. HOLMES: No.

COMMISSIONER BROWN: Your suggestion is that when there is something really important like mutualization, they have found money so that it does not affect their surplus, but for trading they would not let it inhibit them?

MR. HOLMES: Yes, I think there was a tremendous appeal to both policyholders and to our salesmen in the mutualizations under the conditions we went through. In our case I found my biggest support on mutualization from our American managers who did not want the company to be American owned, peculiarly enough, but that was exactly the case, and there was a big support for taking your money then when you could get it and having the company run as a real insurance company.

MR. POYNTZ: Mr. Chairman, I think we should point out that some companies even though they favour the amortization principle for a certain portion of the assets, nevertheless do not overlook the market value situation as well. I think all companies are aware from time to time throughout the year of the total market value of their assets and do report that to the board even though they may favour the amortization principle as a standard for valuing assets -- at least a certain part of them -- and they do a vast amount of trading as well, even though they may be using amortization for part of their assets.

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COMMISSIONER BROWN: Have you any positive suggestions as to any method by which this question of valuation could be altered so as to reduce some of these rigidities?

MR. BRYDEN: Mr. Tuck, that was discussed at the legislative changes last year -- or, Mr. Lemmon, would you like to comment on it?

MR. LEMMON: I am not sure what Mr. Brown is driving at. There are certain rigidities come in through book value accounting. Perhaps I could go into that for a moment. In the last several years most companies have been in the position where the market value of the bond section of their portfolio has been below book value, whereas the market value of the common stock section of their portfolio has been above. In most years the excess has been more than sufficient to carry the deficiency. The problem always comes when you sell out a fairly large portion of your bond account for trading purposes and establish book losses: Should you correspondingly sell out a corresponding portion of your stock portfolio so it doesnot affect your surplus in the one year?

COMMISSIONER MACKINTOSH: Do you wish you had, or not?

MR. LEMMON: I think all companies have done it to a degree, some to a greater degree than others, but our auditors in drawing up our statement, in our particular case, seem to put great stress on the fact of being able to state our assets are valued in total at amortized cost or less and that, in effect,

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makes it necessary to put through a sale to realize a profit to offset a loss, if you are going to do it, and sometimes there is a greater disinclination to do that than others.

COMMISSIONER BROWN: I was thinking about whether there was some way you could set it up as a special fund to be reimbursed by investment? Say you sell a 3 per cent bond at discount, which is attractive to certain people because of tax advantage, and replace it with a 6 per cent bond at par: You have that additional 3 per cent income which quickly recaptures the loss you have taken. Has there been any suggestion you set it up on the books to take care of this?

MR. LEMMON: Yes, we have discussed this at various times with the Superintendent of Insurance and with our auditors, and neither one of them are in favour of it.

MR. POYNTZ: Mr.Chairman, there is a table at page 48 that I think has a bearing on this question: Table 4. h Gross Acqisitions of New Canadian Investments. This is a sample of 12 companies holding 76 per cent of life insurance assets in Canada. You will see the total net investment in a year is considerably less than the total acquisitions even excluding federal governments, so as to exclude the short-term securities that may be rolled over several times in a year. So, there can't be too much inhibition from this rigidity we are speaking of. In 1961 total acquisitions were one billion one hundred and sixty-five million compared to the total net investment of

499 million.

COMMISSIONER BROWN: Except that there would be quite a roll-over on short-term municipal maturities and also the mortgage business.

MR. POYNTZ: I don't believe mortgages are included here, and the short-term Governments are excluded. I don't think there is very much roll-over in Municipals. There is some.

You see the ratio B to C: Total Acquisitions Excluding Federal Governments, the ratio is 2.3 to 1 in 1961, and that is one of the lower ratios.

COMMISSIONER BROWN: May I just get back: This morning I made the mistake of asking a question that was answered in the brief, and I think if you look at page 50 you will find these figures.

MR. McCARTHY; All maturities are included in those tables.

COMMISSIONER BROWN: Including mortgage maturities?

MR. McCARTHY: Yes.

MR. BRYDEN: I am sorry.

COMMISSIONER BROWN: I just feel a little better, that is all. The net investment under bonds is only 182.

MR. BRYDEN: Right.

MR. TUCK: Mr. Brown, the reference to the proposal put forward respecting valuation of assets ---

COMMISSIONER BROWN: Excuse me; whose proposal is this?

MR. TUCK: The proposal of the Association,

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which represented the majority of the views of the companies, is set out on page 42 at paragraph 4.20.

COMMISSIONER BROWN: Yes, this is kind of a half way point between using an amortized basis and the current market basis -- this is using a sliding valuation?

MR. BRYDEN: Yes. I draw your attention to the last sentence:

> "The use of an average of three year-end market values, it was believed would give a more accurate picture of the long-term value of corporate securities and shares and would give the companies time to adjust their balance sheets to new situations."

As you say, it is a half-way proposal.

COMMISSIONER BROWN: Would this contribute to rigidities or not?

MR. LEMMON : We think it would contribute to -- part of the disinclination to invest in ordinary shares is due to a market break, such as we saw this spring, hitting you just on the valuation date, which could make a rather serious impression on the surplus of any company who had a substantial portion of their assets in ordinary shares, whereas if you were insulated against that particular type of thing by a three-year average, many of the companies would be more inclined to participate in equities to a greater extent.

COMMISSIONER BROWN: How about a quarterly average on the current year?

MR. LEMMON: Any sort of average would be

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COMMISSIONER GIBSON: I take it this is not a unanimous view?

MR. LEMMON: Mr. Holmes, I think, has expressed the other view.

COMMISSIONER GIBSON: You say with regard to excluding municipal securities of this country, and Britain, and the United States -- I take it this is not a unanimous view either?

MR. LEMMON: Again, Mr. Holmes expressed the other view. That had another reason behind it: The Insurance Superintendent publishes a book at the end of each year with the market value of all securities held by the life companies. About 40 per cent of that book is made up of the value of municipal securities by the terrific number of municipalities and the number of individual securities issued by each municipality, and it means somebody has to go through and assign an individual value to each one of those and it results in a large volume of work in the Insurance Department and in the companies' offices themselves. We are wondering if it makes a real contribution when the market value of most of these securities is a matter of conjecture, anyway.

COMMISSIONER BROWN: In other words, you would rather have a yield basis fixed for each municipality?

MR. LEMMON: Would that be an improvement, do you think? You would still have the work to do of translating that into the price and extending it

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COMMISSIONER GIBSON: It only arises when some of these securities may be a little less than good -- then you have a problem?

MR. LEMMON: That is quite right.

MR. BRYDEN: In our particular company, for pure accounting purposes we have a tendency to write down all municipal securities to par immediately after, and that does away with all the bookkeeping of amortization. On the other hand, any we buy below par we tend to just let sit, and it very well does away with a considerable volume of work. It does not do away with your valuation problem at the end of the year.

COMMISSIONER GIBSON: It seems to me this accentuates your valuation problem.

MR. BRYDEN: You have got to relate each individual price to that particular par value of the securities which you hold.

COMMISSIONER GIBSON: We might go on to the distribution of your assets. Table 4.f, I guess, at page 45 is the essential thing, showing the proportion of assets in various categories. This is a very interesting table to which a number of references have been made today.

First, on a rather minor point, the ratio of cash has climbed gradually over the years despite the fact your cash inflow must be steadily increasing. Does this mean better money management and the development of the short-term money market?

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MR. McCARTHY: That is the answer, sir. As the money market has developed in Canada the companies have more efficiently employed their short-term cash balances.

COMMISSIONER GIBSON: Is it general practice for the insurance companies now to carry a sizeable amount of money market securities off and on so they can be fully invested?

MR. McCARTHY: How do you mean that? Do we carry a larger total cash position than formerly?

COMMISSIONER GIBSON: No; you obviously carry a smaller cash position. Do you carry quite a lot of these liquid instruments so you are able to move quickly?

MR. McCARTHY: I would say the answer is yes; we are more inclined today as a group in the face of expectations of higher interest rates to accumulate a larger liquid position in the form of money market securities than was the case before the money market developed.

COMMISSIONER GIBSON: Do you do this when you see interest rates are rising, or the market is going down, and on the reverse you use the selective basis?

MR. McCARTHY: Quite.

MR. BRYDEN: I think there is also the point that has to do with our future commitments on our mortgage accounts, because there is quite a seasonal trend in the advances, and it could be at times you may go into a short-term money market position

pending the time you expected a rather substantial outflow of mortgage account, and that is another reason for more and greater use of this short-term instrument.

COMMISSIONER GIBSON: Some of these may mean a maturity of 6 or 8 months, and a year; they were not necessarily all treasury bills?

MR. BRYDEN: That is right.

COMMISSIONER GIBSON: Now, these sort of major trends in this thing are reasonably clear: There has been a reduction relatively in the total holdings of bonds, share bonds in your total assets, and a quite sharp reduction in the share of Canada bonds, and a marked increase in the share of corporate bonds, though that is looking at it over a longer period; and a big increase in mortgages. Is this a pattern, or does it mean very much? I am talking really about the differences between one company and another. If you take 8 or 10 companies with their annual statements, the differences are really terrific in some of them, and you refer to them in the brief from time to time. Have there been any trends in recent years? Have some companies gone one way and others gone another way, or are these changes meaningful when you look at the whole pattern -- that is, more mortgages and less bonds.

MR. BRYDEN: As a completely general statement to start with, the companies during the war certainly increased their holdings of federal government bonds and at the same point you had your mortgage accounts running very significantly down. Then, I think once the postwar period developed there was this demand for

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housing and so on and most of the companies attempted to increase their mortgage portfolios. That accounts for , in part,the rundown on the Federals, and then you reached the point ---

COMMISSIONER GIBSON: Excuse me, when was that finished -- about 1950 or so?

MR. BRYDEN: I would say about 1957, I think, would have put the end to that, and from about 1957 on the total of our mortgage loans as a percentage of the total assets has apparently reached a plateau. That still does not explain why different companies have different approaches to this. Perhaps Mr. Lemmon could add something to this.

MR. LEEMMON: I don't know that I can add much to that except to say there is no unanimity of judgment as between the investment committees of the companies as to what distribution of assets they should have at any given moment. Some companies are more mortgage minded than others and want to put a higher percentage of their assets in mortgages. Other companies feel that in spite of the fact securities perhaps have a slightly lower running yield than do mortgages, there are other opportunities of trading and that sort of thing that enable you to more than make up that gap.

COMMISSIONER GIBSON: Would it generally be true that most of the companies have been reducing their holdings of Government of Canada bonds over a good many years?

MR. BRYDEN: I think that is fairly evident.

COMMISSIONER GIBSON: I notice in the record

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COMMISSIONER GIBSON: Excuse me, when was that finished -- about 1950 or so?

MR. BRYDEN: I would say about 1957, I think, would have put the end to that, and from about 1957 on the total of our mortgage loans as a percentage of the total assets has apparently reached a plateau. That still does not explain why different companies have different approaches to this. Perhaps Mr. Lemmon could add something to this.

MR. LEMMON: I don't know that I can add much to that except to say there is no unanimity of judgment as between the investment committees of the companies as to what distribution of assets they should have at any given moment. Some companies are more mortgage minded than others and want to put a higher percentage of their assets in mortgages. Other companies feel that in spite of the fact securities perhaps have a slightly lower [illegible] yield than do mortgages, there are other opportunities of trading and that sort of thing that enable you to more than make up that gap.

COMMISSIONER GIBSON: Would it generally be true that most of the companies have been reducing their holdings of Government of Canada bonds over a good many years?

MR. BRYDEN: I think that is fairly evident.

COMMISSIONER GIBSON: I notice in the record

here this goes on really through 1958, through the conversion, then they start to increase a bit in 1959. There are some quite substantial purchases in 1959. Would you care to comment on that period?

MR. LEMMON: I think any comment on that would have to be very general. You will probably remember the pattern of the Dominion market better than I do but the Dominions at the end of 1959 and early 1960, as you may remember, ran into a very difficult time market-wise and got down to what appeared to many companies as a pretty attractive yield basis, when the 5½ per cent convertibles were issued and the famous C.N.R. 5 per cent issue sold at very substantial discounts, and I think the companies were fair buyers of Dominions at that time, which was a very difficult market for Dominions. That shows up in the increase for 1959 and early 1960.

COMMISSIONER BROWN: They were sellers in the last quarter of 1959 -- this is page 52.

MR. LEMMON: You have to take that one apart and analyze it. There is always a little bit of window dressing goes on by companies on December 31.

COMMISSIONER BROWN: Perhaps we should ask about this cash thing too -- the end of the year is probably the high point for cash.

MR. LEMMON: It could be.

MR. BRYDEN: Yes, pretty generally.

COMMISSIONER GIBSON: In 1958, in the second and third quarters you were selling Canadas and heavily buying corporate bonds, and then later in

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COMMISSIONER GIBSON: In 1953 in the second and third quarters you were selling Canadas and heavily buying corporate bonds, and then later in

the fourth quarter you were buying Canadas and selling corporates, and the first quarter of 1959 you were heavy buyers of every kind of bond. Would you care to make any comments on that movement into corporates in 1958? Were the corporate bonds a considerably better yield level and the spreads wider than usual?

MR. LEMMON: My memory is not that keen, to tell you the truth, but the purchases of corporate bonds tend to come when corporate bonds are available. When there is a large volume of corporate financing the companies tend to be heavy purchasers of them and when there is not it is pretty hard to pick them up in the secondary market in sufficient volume.

MR. HOLMES: There was quite a period when, if corporations wanted to finance, they had to pay the price, and the governments would fall to a fictitious level. We could not very well hold them under those conditions.

COMMISSIONER GIBSON: It is hard to draw any conclusion from this because there is nothing on maturity distribution of these bonds. Have you got any sort of picture of the maturity distribution in your Canada holdings now or would there be quite a spread.

MR. McCARTHY: I would think that would vary, sir, from company to company.

COMMISSIONER GIBSON: You do not think it would vary?

MR. McCARTHY: I think it would vary from company to company. I would think actual portfolios in the industry today are shorter than they were in late 1958 and early 1959 from my own experience.

COMMISSIONER GIBSON: In which you were holding a portion of them as a fund to be used as you saw fit as opportunity arose?

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MR. McCARTHY: Yes.

COMMISSIONER GIBSON: But the emphasis of your investments in bonds is still on long maturities?

MR. McCARTHY: Yes sir. I should make another observation. You were commenting on the switch away from mortgages into bonds in late 1958 and early 1959. The mortgage portfolio, I think you understand, really is not a long term type investment; it is a pretty short term type investment and in that period when bond rates were fairly close to mortgage rates companies had a large bond account. Those rates, that is, the corporate ran for a very long period of time and I think in large measure that explains the sudden change to bonds and away from the mortgage end.

There are two aspects of this problem, that is, current rate and how long you will have it. This was one time that we seemed to have a historically high rate assured for a very long time, a rate very close to the mortgage rate.

MR. BRYDEN: Mr. Gibson, on your matter of maturity I have a portfolio here. This is a bond and debenture account. It is not just limited to federal bonds but it is a sample of the type of maturity that does exist. In this case five years or less represented 7.6 per cent of the total bond and debenture issues, five to ten years was about 12½ per cent, ten to fifteen years about 22½ per cent, fifteen to twenty would be about 32 per cent, twenty to twenty-five almost 14 per cent, and over twenty-five

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about 11 per cent.

COMMISSIONER GIBSON: The short maturities would be the higher proportion of the Canada bond, would they?

MR. BRYDEN: They would be Canada bonds and possibly maturing municipals.

COMMISSIONER BROWN: And corporates?

MR. BRYDEN: I doubt if we would hold the corporate bonds down that long. As a rule they are sold prior to that point.

MR. HOLMES: There are a lot of these corporates, would they be in there?

MR. BRYDEN: Yes, as far as we are concerned.

MR. RAPSEY: I took a look at the position in the second and third quarters of 1958 and our experience followed this pattern pretty well and our acquisition of bonds was kept down in one year to notepaper. In effect, what we were doing was looking after mortgages and real estate commitments and we were selling the long government of Canada bonds without going out of line at that time.

COMMISSIONER GIBSON: In other words, when you delved into the future interest rate structure you dealt more in mortgages and had a good yield?

MR. RAPSEY: We had mortgage commitments and in order to provide for them we were moving out of governments and putting the money into shorter term industrial paper.

COMMISSIONER GIBSON: One general point on the way that insurance companies invest. It is

stated from time to time that an insurance company has a quota for municipals and has one for mortgages and various types of securities. Is this general practice that quotas are set and adjusted from time to time?

MR. BRYDEN: Mr. Chairman, I do not know how general it is, but I would assume that most companies would make some projection as to the growth in their assets during the coming year. I should probably go so far as to say put in the light of the knowledge of the markets, what your ideal distribution should be. That produces, after your estimated repayments, a cash flow into these particular categories.

Now, as far as we are concerned on mortgages, for example, where we were content to put in new money to the extent of 50 per cent of our increase in assets that still produced a total new investment in mortgages in a year which is less than a mortgage organization could reasonably produce. So at that point we have to say to our branch officers, "Well, for this year here is your new quota for approvals on mortgage accounts", and I would think most of us operate in some fashion of that kind.

COMMISSIONER GIBSON: But this is another reason to bring this up, the quite possible rigidity in response. When companies run out of a quota or target or whatever you call it, the limitation set for each group of investments in the year, is it common to say: "Well, we have not any more to put in this area this year, you will have to wait until next

year"? Would you describe the possibilities there?

MR. BRYDEN: That would depend on what changes were taking place within the market. You do not set up projections for a year and then let them sit. If there is some change in the market levels, interest rate levels, et cetera, then you vary this ideal proportion which you set up for yourself as a target for your investments so that it might be that your mortgage branch office might say: "Well, I am sorry, nothing until next year". On the other hand, if there was some change that made additional mortgages more attractive then there would be differences in your quotas given to these branches.

COMMISSIONER GIBSON: You might change your program?

MR. BRYDEN: Yes.

COMMISSIONER GIBSON: That would take a bit of a push; it would have to be a fair market to induce you to do that?

MR. BRYDEN: I am not so sure. Sometimes it appears to me it has not taken too much.

COMMISSIONER BROWN: Do you vary it considerably between federal and provincial or provincial and municipal? You might say: "Sorry, nothing is left for municipals".

MR. BRYDEN: You could, but I am not so sure it would be refined to that extent. You would operate between, say, your mortgage account on one hand and your bond account on the other, and your stock account.

If there were significant spreads between municipals and, say, provincials I think they are taken care of in just the normal purchasing that you do because I think people pretty well tend to look at municipals and provincials to a very great extent as being the same sort of an animal.

COMMISSIONER BROWN: And on your mortgages you give an example that you kind of ran out of mortgage money. Would you then say: "Well, we will make more money available and increase it one-half of one per cent"? Would you change your rates or wait for the market to change?

MR. BRYDEN: I think we would wait for the market because my guess is you would not have any takers at the one-half per cent additional if there had been other institutions still with mortgage money to loan. I would not say it would take a significant change in the market to do that.

COMMISSIONER BROWN: Presumably we are talking about North American?

MR. BRYDEN: Yes.

COMMISSIONER BROWN: I wonder if any of the other companies have different patterns.

MR. BRYDEN: I would be happy to have what I have said supplemented.

MR. HOLMES: We do not do much spending. We have to give them some sort of quota for mortgages but we are inclined to stiffen our terms rather than run out of mortgages if we are getting more than we think we want, but if we are getting them very freely

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we are inclined to stiffen our terms.

COMMISSIONER BROWN: Would you put your interest rates up before North American found out?

MR. HOLMES: Well, we would get a certain amount of business even if we did.

COMMISSIONER GIBSON: Do you by some method ration it out rather than say: "We are sorry, we are not going to do any more"?

MR. HOLMES: To some extent. In this year you will find they are lending next year's money.

COMMISSIONER BROWN: At this year's rates?

MR. BRYDEN: At next year's rates.

MR. RIEDER: I think our industry is very much the same as that of Mr. Bryden's with this addition, that we always caution our branches not to run out during the year.

MR. BRYDEN: We do that too.

COMMISSIONER GIBSON: There comes a time when you see good opportunities for bonds, and the mortgage demand is strong and you are running over your quotas right across the board -- what do you do then?

MR. BRYDEN: We can only invest the money we get.

MR. POYNTZ: Then you do have to ration.

COMMISSIONER GIBSON: Do you do this by saying "Since the rate has been down we will only take so much"?

MR. RIEDER: You will not be alone because the industry will feel the upward movement.

COMMISSIONER GIBSON: But you are an important factor in this industry you are talking about and I would think you would exercise leadership in the kind of policies you follow.

MR. RIEDER: That would indicate a demand for increased mortgage money and therefore the rate would go up.

MR. HOLMES: It really does not take them very long. As a matter of fact, they went up several times to 7½ per cent and we stayed at 7½ with other companies below us for a year and got a fair amount of mortgages. If we were not getting too much, we came down.

MR. POYNTZ: We had very much as Mr. Bryden described. We set up a program at the beginning of the year and a target, so much to mortgages, so much to bonds, and it could vary two or three times during the year. Each year altered depending on the relative traction of the various types of securities available.

COMMISSIONER GIBSON: Mr. McCarthy, would you like to say anything about this?

MR. McCARTHY: In our company, sir, we sit down once a year and make a determination of what we want to do in the mortgage field. It is as much an administrative effort as anything else. You have a mortgage organization and they have to know what they have to spend in the time ahead. This determination is made in the light of the best expectations we can summon up about the nature of the year ahead and if

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the conditions change considerably, or perhaps not terribly considerably but materially from what we had envisioned, we are quite flexible in either adding to or subtracting from a mortgage program already outlined in the first instance.

COMMISSIONER GIBSON: And in raising your rates, if the general demand is increasing?

MR. McCARTHY: Well, the investment area is really divided into the conventional and N.H.A. and the first area to bear the brunt of the rising rate situation is obviously the N.H.A. if your conventional rates are beginning to go, and I think most of us are sensitive in this area and we will attempt to get a better rate. If it falls away from the N.H.A. rate to a significant extent there is a tendency then to consider an allocation between the two areas to the detriment of the administrative rate.

COMMISSIONER LEMAN: Over the past years what has been the trend on conventional mortgages? The demand has been high most of the time.

MR. McCARTHY: Most of the time.

COMMISSIONER GIBSON: What happens in a corporate bond market when there are a lot of issues becoming available and money is getting tight? Do you take as much as you can and then stop or do you raise the rate at the same time?

MR. McCARTHY: If they are as attractive as that we recognize one factor of life in the corporate bond market mentioned here before that you buy them when available as new issues, and that is really the only

condition in which you can make significant progress on your corporate bond portfolio and if they are that attractive relative to other criteria obviously once you have exhausted available cash you will make commitments against trading possibilities and at the final analysis if they are all that attractive you will attempt to arrange your commitments for previous downgrow at the rates that prevail at the moment and you will increase your forwards if the nature of the demand permits that.

COMMISSIONER BROWN: Delayed delivery.

MR. McCARTHY: Delayed delivery.

COMMISSIONER GIBSON: Do you think in terms of rationing these bonds between applicants or raise your rates and prices to some of the applicants?

MR. McCARTHY: Well, in my own experience it has been the case under extreme demand for bonds that there will be some rationing in terms of the amount of each individual one that we can buy, if we can clearly see that there was anything more behind them, and that this condition was likely to prevail. This raises the problem that you cannot detail that very well because in Canada you have no clear forward view on corporate bonds. There is no such thing as a calendar of firm borrowings and borrowers seem to be in some instances almost secretive in going to the market, moreso under the conditions you describe. This produces surprises. You would tend to, under those conditions, ration or limit your participation on each one that came along, and as you can see this is not a precise science,

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you have not got enough information.

COMMISSIONER GIBSON: You would rather spread the fund out and raise the price or have a higher interest rate?

MR. McCARTHY: It is in the nature of the publicly offered bond issues in Canada that the lender, the insurance company, that once the issue has been made, the only way you can influence the rate on the next one is not to take this one. You cannot change the rate on this one.

COMMISSIONER GIBSON: I am thinking about the ones that are coming out.

MR. McCARTHY: If the issue receives a limited response the next one has to come at a higher rate and that is how you get your point across as a lender.

THE CHAIRMAN: We will adjourn for a few moment.

(At this point a short recess was taken.)

--- After recess.

THE CHAIRMAN: We shall now resume.

COMMISSIONER BROWN: This morning we touched briefly on this question of foreign assets against foreign liabilities. I should like to refer to paragraph 5.42. The last sentence reads:

> "(Non-resident companies doing business here are encouraged by the authorities to cover their Canadian liabilities with Canadian assets.)"

What do you mean by "encouraged" ?

MR. BRYDEN: Mr. Westwater might answer that.

MR. WESTWATER: We were encouraged by a letter from the Superintendent of Insurance a year or two ago. There is no statutory necessity to cover everything.

THE CHAIRMAN: There is no necessity for a statute, I take it?

MR. WESTWATER: Mr. McGregor, or else his predecessor, addressed a letter to all the general companies requesting that to as great an extent as possible we should invest our assets in domestic securities. That is the extent of the encouragement.

COMMISSIONER BROWN: What is the situation with respect to the foreign liabilities of Canadian companies? Are they required by the jurisdictions in which they do operate to protect themselves by investment in those currencies?

MR. BRYDEN: I do not think there is any

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real requirement in any place that we carry on business to do so. As a matter of practice we would have well over 95 per cent of our United States assets in United States investments. Within the sterling area -- we are only down in the Caribbean area -- we attempt to match the currency of liabilities with local currency assets, but once again there is no reqirement as such, although there is getting to be a requirement in British Guiana.

MR. LEMMON: The state of New York has a requirement that a company obtaining a license there may not have more than 10 per cent of its assets invested in Canadian securities and one per cent in other foreign securities. That is not a currency provision, that is a debtor provision. That is in relation to Canadian debtor securities and foreign debtor securities.

The situation in sterling as far as the United Kingdom is concerned is that it is not a matter of law, but since 1939 it has been a matter of the Foreign Exchange Control Board. If you wanted to withdraw assets from a sterling area you had to get permission from the Foreign Exchange Control Board, which was not ordinarily granted unless you had an extent of sterling assets over sterling currency liabilities.

COMMISSIONER BROWN: In other words you could move your surplus?

MR. LEMMON: That is generally it. That is not 100 per cent true. There are other circumstances under which it would be permitted, but that is generally

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COMMISSIONER BROWN: I should like to turn to paragraph 5.44. Again this was touched on this morning and has reference to the movement of funds that takes place because of the differential in interest; when spread narrow it moves one way and when it is wider it moves the other way. How much of a change activates the companies?

MR. BRYDEN: Possibly Mr. Rapsey might be our closest trader in that area. What would be your reaction?

MR. RAPSEY: I think it is a combination here really of the interest rate spread and the question of exchange rates that dictates this thing. I would assume that it is a question of the individual companies' opinion as to just the right spread at which to do this sort of thing. I think perhaps we all have the same historical data on which to work, as to what seems to be more or less the normal spread, but I am also sure that we come to all kinds of different conclusions as to how much of a spread we would require to do this sort of thing. I think there have been instances outside the question of moving between here and the States where we have perhaps done a little bit of moving between here and London where interest rates have widened considerably and we have been able to get a much larger rate in London. That has been very, very small. I would not like to say that there is any set figure for doing this sort of thing.

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COMMISSIONER BROWN: There is no rule of

thumb?

MR. RAPSEY: No rule of thumb.

COMMISSIONER BROWN: How about the other companies?

MR. POYNTZ: I do not think we would have a rule of thumb, Mr. Brown. We are concerned only with sterling, United States dollars and Canadian dollars. We have from time to time brought back sterling to the extent of our surplus earnings there. We have not brought back United States dollars recently. We maintain a very low position in United States dollars. We are now beginning to bring that back to Canada, taking advantage of the premium on the exchange and the higher rates of interest available here. There is not a pattern to this activity.

COMMISSIONER BROWN: It is just that you all are responsive to varying degrees as the market changes?

MR. POYNTZ: Yes.

COMMISSIONER MACKINTOSH: I take it that it is not a matter of how narrow the spread is, but to what extent and at what time you expect it to widen again?

MR. BRYDEN: Yes, it is the expectation.

COMMISSIONER MACKINTOSH: It is not something on which any two people would agree?

COMMISSIONER LEMAN: It is probably something they do not want to tell each other, either.

MR.BRYDEN: I wish there was a rule of thumb.

COMMISSIONER BROWN: I wonder if we could

discuss briefly, while talking in the connotation of this distribution of assets, about the investment in municipal securities. This varies from company to company depending on how far they have developed the municipal section of their investment department, but life companies as a whole are probably the largest pools of knowledgeable savings that are directed toward the non-term dollar liabilities and as such probably constitute the logical place for assisting municipal financing. In one section of your submission you refer to moving to provincial, municipal and corporate securities to increase the yield, and yet in paragragh 7.11 you talk about the advantages of provinces extending guarantees to municipalities in order to give them a wider market. This tends to reduce the yield on municipal securities.

MR. McCARTHY: These two points are made in the brief. I think what we haveto draw your attention to is this. The industry has been an will likely continue to be an important buyer of municipal securities, but they will only buy municipal securities that merit their purchase. There are a group of municipalities in Canada; they may vary from time to time in numbers and in total dollar needs on the capital market, that for one reason or another do not measure up to the standards that the industry requires. We say that this group perhaps could be handled better by the provincial pooling arrangement. Do you see the point?

COMMISSIONER BROWN: Yes, but by "pooling"

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COMMISSIONER BROWN: Yes, but by "pooling "

do you mean just a municipal pooling and issuing something as a pool, or do you mean some sort of provincial guarantee?

MR. McCARTHY: Provincial assistance; provincial borrowing on the capital market and advancing the money to the municipality on a basis like the exchanges of securities, perhaps, until such time as the muncipality can go to the market on its own merits.

COMMISSIONER BROWN: This means the existence of a lower yield ?

MR. McCARTHY: It would mean that the insurance company would look at the provincial guaranteed credit and would make its mind up, as it does all the time, as to whether or not at that particular time that particular guarantee was an acceptable investment.

COMMISSIONER BROWN: You are putting it on the basis of a provincial guarantee rather than on the basis of the municipality itself?

MR. BRYDEN: Yes, but under these conditions this particular municipality probably would not be buying at all. So, to that extent the addition of this additional credit gives them access to the capital market which otherwise might have been denied because of their own particular credit position.

COMMISSIONER BROWN: So the poorer municipality gets money on a cheaper basis? The municipality that has a poor credit gets money on a cheaper basis than the other municipality that borrows directly?

MR. McCARTHY: It all depends. A provincial

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MR. McCARTHY: It all depends. A provincial

jurisdiction could lend money to a municipality at a higher rate if it chose to do it. The province borrowing the money could advance it to the municipality directly rather than the municipality coming to the market with a guarantee of the province. There is more than one way of doing it.

COMMISSIONER BROWN: You do not think the insurance companies with their large pools of funds could satisfactorily spread the risk to look after some of these lesser known municipalities?

MR. BRYDEN: It is not a question, Mr. Brown, of necessarily being lesser known. I think basically it is a question of their credit worthiness; whether they have the economic background, assets and so on to service the debt. In other words, these are municipalities which may lack sufficient credit.

COMMISSIONER BROWN: Well, that is the point I was getting at. It is not a question of knowledge?

MR. McCARTHY: It is a question of credit worthiness.

COMMISSIONER BROWN: It is a question of the credit worthiness of the municipality itself?

MR. McCARTHY: Yes.

COMMISSIONER BROWN: And you are prepared to buy municipal bonds of an unknown municipality providing it can be shown that the credit is justified?

MR. BRYDEN: Yes.

MR. LEMMON: Yes.

COMMISSIONER GIBSON: Is the interest of insurance companies in regard to municipal bonds

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MR. [illegible]: Yes.

MR. [illegible]: Yes.

COMMISSIONER GIBSON: Is the interest of insurance companies in regard to municipal bonds

increasing with the development of larger municipal areas like the bigger school districts in the West and so on, and the greater interest on the part of provincial governments in providing standards for municipal grants? Is this increasing the demand for municipal bonds on the part of insurance companies? We have heard a lot about this across the country.

MR. BRYDEN: On page 66 in Table 4.0 we have tried to set out here the participation of the large insurance industry in municipal bond issues in Canada. It covers the figures from 1952 through 1961, and it shows the net purchases by the life industry of the net new issues of municipal direct and guaranty bonds. You will notice that the per cent of participation varies from year to year, but in 1961, for example, life insurance companies bought 18 per cent of all the new municipal issues offered.

COMMISSIONER GIBSON: It is a higher variable percentage, is it not?

MR. BRYDEN: Yes.

COMMISSIONER GIBSON: I notice your portfolio, as a proportion of your assets, has stayed fairly stable in the postwar term.

MR. BRYDEN: Well, yes, I think it has stayed quite stable, but one point I think that must be borne in mind is that the life insurance industry can only invest really its net increase in assets in any year. To the extent you go into a certain area you must reduce some other area. It is a matter of shuffling within a certain total. You try to cover as wide a

spectrum of the reasonable needs as you can but there is a limit beyond which the money just is not availble.

COMMISSIONER GIBSON: It is not one of the areas growing rapidly becuase of this increase in housing and so on? Are you participating to an increased degree in housing?

MR. BRYDEN: Yes, and we have felt that rather than go any further in housing we had some sort of responsibility to help provide the amenities that make housing feasible. That has been one of the reasons for the increasing interest in municipal bonds.

COMMISSIONER BROWN: If I remember rightly some companies have a rule of thumb that they will not invest in any one municipality more than X dollars per capita, relating to the population of that municipality. Is this general?

MR. BRYDEN: I would not say it was general. We try to work out some kind of a yardstick as to the amount that we would like to see in any one municipality. The easiest method seems to be to relate it to the number of people in the municipality so that we do have limits of that character. The limits are pretty much $10 per capita in the municipality of any substantial size, so with 50,000 people it would give you $500,000 being the top limit in that municipality. Now, the chances of building it that high in a number of those cases is pretty thin. Those limits are beyond what you would probably have by distributing your municipal portfolio over the number of municipalities which you own.

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COMMISSIONER BROWN: The municipal issues now in all provinces are largely issued in serial form except for the large metropolitan areas. This historically I think came about because of the problems that arose through sinking fund maladministration in the 1930's. Have life companies had any second thoughts about the advantages and disadvantages of serial issues as against sinking fund issues of municipalities?

MR. LEMMON: No, I would think on the average we still think the serial method is the best method by which to finance. We do realize that that proposes some limitations in the marketability of those bonds, because to individuals small serial maturities are not particularly attractive. We still think that is best, and we still do not like the idea of small municipalities getting into the problems of sinking fund administration.

There is another alternative, of course which is a sort of pooled sinking fund arrangement, but that seems to create more problems than it solves. I think most of the companies would still lean toward serial maturities for municipalities.

MR. McCARTHY: Our company has been investing in municipal bonds for a very long time. We would agree with that statement while recognizing that it runs perhaps counter to one or two other objectives. The objective is to secure as long-term as possible, for instance, on your fixed income securities, but in the interest of public finance administration of the small and medium type municipality we would tend to feel on

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the basis of our own experience and judgment that the retention of the serial form is the best.

COMMISSIONER BROWN: Everyone is unanimous in that regard?

MR. BRYDEN: I would not disagree.

COMMISSIONER BROWN: How about a rating for municipal securities similar to the system in the United States?

MR. McCARTHY: I think most of the companies that have been in the municipal business for a long period of time have individually developed some form of a rating system; some more comprehensive than others. As far as a publicly or privately operated rating system, I do not think we would regard it as being very useful. I think we would use our own methods because they have been proven and proved satisfactory.

MR. BRYDEN: You may remember, Mr. Brown, that was one of the things that the Citizen's Research Institution did in the past. That institution rated municipal bonds, but it finally just petered out. There was not enough call for it and it is defunct as of now.

COMMISSIONER GIBSON: I would like to ask a few questions about mortgage preferences in insurance companies. Mr. Lemmon said earlier that 66-2/3 limit on conventional mortgages was one of the few restrictive limits in his view

COMMISSIONER GIBSON: Is that a fairly widely used element? In other words, that loans may be made at a higher percent?

MR. McCARTHY: I think that generally speaking the restriction does prevent some lending. In my own experience it would not be too significant in the total scheme of things. I think if the limit were higher that most of the companies would tend to propose that the majority of trade loans observe something around the two-thirds ratio.

COMMISSIONER GIBSON: There would be situations where it would be convenient to get rid of this particular thing?

MR. McCARTHY: That is right.

MR. POYNTZ: It probably would not mean that more money would go into the mortgage market, though.

COMMISSIONER BROWN: It probably would mean that you would loan on fewer houses?

COMMISSIONER GIBSON: You could make more large corporate mortgages?

MR. LEMMON: Yes.

COMMISSIONER GIBSON: That is an interesting observation. Of the loans that are made on existing residential properties, what parts are associated with transfers of such properties and what part is for other purposes? In the first place, do you make many loans against the existing residential properties, not new homes?

MR. BRYDEN: It is a fairly significant part

of most companies' business. Usually I imagine it takes place at the point at which the property is being sold to another purchaser, so it helps finance the sale.

COMMISSIONER GIBSON: In some of these you make mortgage loans to people who simply want money for a use, it is not to finance a sale at all?

MR. BRYDEN: Yes, I think that you would do that from time to time. There it bears on how you assess the value of the house and his credit, and presumably at that point you would probably ask him what he wants the money for and to see if it is a perfectly good risk. The chances are that you would do it.

COMMISSIONER GIBSON: Whether or not this is a good asset; that is the main point is it not?

MR. BRYDEN: That is right.

COMMISSIONER GIBSON: The loan is in proper relation to its value, so you do not care too much what is done with the money?

MR. LEMMON: No.

MR. RIEDER: I would say it is not a very significant part of our operation for the financing of old houses; perhaps 80 per cent is N.H.A. and that is on new housing and it would be a fraction of the rest.

MR. BRYDEN: If the Commission is interested, Dominion Mortgage and Investment have figures of the breakdown on loans made by the life company members by new houses, existing houses, and so on; I do not happen

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COMMISSIONER GIBSON: We would be very interested in that.

MR. BRYDEN: We will send it along to the Secretary. Would you want this for a one-year period or what?

COMMISSIONER GIBSON: As it appears in the latest period.

MR. BRYDEN: Would you want just the latest period or a period of years back?

COMMISSIONER GIBSON: It would be interesting to see if there has been any change.

MR. BRYDEN: We will give it back as many years as we have it available.

COMMISSIONER GIBSON: Do you think there is much demand in this area for existing houses; is there an area where finance is needed here? We have had suggested to us by a number of people that there is not enough money available on existing properties.

MR. McCARTHY: I think one point that has to be made is that to the extent that the insurance industry were to devote significant funds to the financing of old houses that it would be just that much more money not available for the construction of new houses, and that aspect has to be related to public policies, and so on. You do not add much to employment and income by refinancing old houses.

COMMISSIONER GIBSON: And it is usually an individual operation, whereas the financing of new houses is usually done with a builder, so that you

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COMMISSIONER GIBSON: And it is usually an individual operation, whereas the financing of new houses is usually done with a builder, so that you

are really moving from wholesale to retail in a sense?

MR. POYNTZ: I think the companies are interested in lending on existing houses to facilitate a sale, but the pressure may be felt by the purchaser who may not get as high a ratio of loan to value as he might wish. I think there is money available, but not on the same terms, possibly, as for a new house.

COMMISSIONER BROWN: There would be a higher proportion -- would this in fact increase the price of the old house?

MR. POYNTZ: I think it would.

COMMISSIONER BROWN: So that would not be any advantage to you.

MR. POYNTZ: I doubt it.

COMMISSIONER BROWN: The advantage would be to the seller.

MR. POYNTZ: Yes.

COMMISSIONER MACKINTOSH: The buyer would get a house and the seller would sell his house and they both get some advantage out of it, but I would think the greatest concern in this is in the mobility and the difficulty of moving people because they have houses which they have to sell and if they have to buy an existing house they only get a two-thirds mortgage on it and are scrambling around for all sorts of odds and ends of finance to try and get the rest of it, and they are often quite young people in communities where you cannot resell the house. It is quite a problem in the mobility of high class estates

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Now, I want to ask the question if 66-2/3 is a little low, how high is comfortable?

MR. BRYDEN: Well, I do not think, Dr. Mackintosh, that the industry has a view on that subject. I think that for pure practical lending purposes that there are times when you could quite easily feel that the security was such that you could go to 75 per cent. There might be other times when the security is such that you would not want to loan beyond 50 per cent. As far as the industry is concerned, we were in thorough agreement at the point at which 66-2/3 per cent was stated. I think some of us may feel that if we made a mortgage loan larger than that that we might put it in the basket, but that was denied to us under current legislation.

COMMISSIONER MACKINTOSH: You do say at one place that you are going to suggest the 80 per cent for the home owner.

MR. LEMMON: That was under the National Housing Act.

COMMISSIONER MACKINTOSH: No, I think that was on existing houses and limited to the purchase by a home owner.

MR. LEMMON: That is in the case of the National Housing Act with regard to existing houses. It was not suggested as a conventional loan.

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What happens though to all this money that is drawn out by the seller? Is it maintained in savings form or spent currently? I think this is one of the problems where it exists in making it too easy to get too large a loan on existing houses.

COMMISSIONER BROWN: What would the reaction be to an adjustment to this basic clause to take care of a surplus of 66-2/3 per cent on any mortgage?

MR. LEMMON: Some companies were in favour of that at the time of the revision of the Act. I do not know whether that was all the industry, but certainly companies were in favour of it.

MR. BRYDEN: I do not actually think it was unanimous.

COMMISSIONER BROWN: What would be the argument against it if the company wished to use the basket clause for this purpose?

MR. TUCK: I do not think any company did speak

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MR. BRYDEN: I guess it was a unanimous view.

COMMISSIONER GIBSON: Do you really think a great many people would start monetizing their equities in their houses and go rushing off spending it? It is a great advantage having an equity in a house from a tax point of view.

MR. BRYDEN: But on the other hand, you continually get the situation in certain locations where there are individuals who know the house's age and to the extent that you allow too high a mortgage, but you do free a lot of cash which at the moment is locked up pretty well.

COMMISSIONER GIBSON: But it is deliberately locked up as a matter of conscious choice; that person has built up an equity in that.

THE CHAIRMAN: You say that there is a tax advantage to this?

MR. BRYDEN: Yes.

THE CHAIRMAN: I do not see what difference it makes; supposing he does decide to spend the money, suppose he is a retired person and decides that he will just spend that money and have none of it left by the time he dies, what difference does it make? Why should he not be able to do that?

MR. HOLMES: You have to take over the house and sell it. There is not a fixed price for it and there has been a varying price for the last couple of years. We have moved three men out of Saguenay and had to take

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over their houses at lower than they paid for them, and we still own those three houses. If you were thinking of 80 per cent loans, they are risky loans to make.

THE CHAIRMAN: I think that would be so, as you pointed out here you would have to be very careful as to the evaluation, but why shouldn't houses be more liquid than they are? That is, older houses. There are many people living in an older house and they have to move for some reason to some other part of the city or some other city and they have great difficulty in selling the house, financing the sale, and if mortgages were available for that sort of thing I would think it would be well worthwhile. It may be entirely different from the point of view of a life insurance company; it may not be considered a convenient type of interest.

MR. HOLMES: When you are thinking of somebody else loaning them the money -- you have to think of a person loaning the money, and they have to get something for it if you are going to get anything like 80 per cent.

THE CHAIRMAN: It is on a fairly low evaluation --

MR. HOLMES: The N.H.A. has gotten people's minds fixed on a 6½ per cent rate and an 80 per cent loan. That would not be the case if you were loaning on old houses at these values.

THE CHAIRMAN: Well, in terms of loaning at these particular values, it is a question of having some sort of a mortgage market for existing houses, and it may be an entirely different -- you may decide

over their houses at lower than they paid for them, and we still own those three houses. If you were thinking of 80 per cent loans, they are risky loans to make.

THE CHAIRMAN: I think that would be so, as you pointed out here you would have to be very careful as to the evaluation, but why shouldn't houses be more liquid than they are? That is, older houses. There are many people living in an older house and they have to move for some reason to some other part of the city or some other city and they have great difficulty in selling the house, financing the sale, and if mortgages were available for that sort of thing I would think it would be well worthwhile. It may be entirely different from the point of view of a life insurance company; it may not be considered a convenient type of investment.

MR. HOLMES: When you are thinking of somebody else loaning them the money -- you have to think of a person loaning the money, and they have to get something for it if you are going to get anything like 80 per cent.

THE CHAIRMAN: It is on a fairly low evaluation

MR. HOLMES: The N.H.A. has gotten people's minds fixed on a $6\frac{1}{2}$ per cent rate and an 80 per cent loan. That would not be the case if you were loaning on old houses at these values.

THE CHAIRMAN: Well, in terms of loaning at these particular values, it is a question of having some sort of a mortgage market for existing houses, and it may be an entirely different -- you may decide

to loan up to the full amount but you might not be entitled to it.

COMMISSIONER MACKINTOSH: As to monetizing the proceeds of a higher mortgage on an existing house, what happens to the fellow who has a house that he has built at the 60 per cent equity, would you monetize that part he had built up in equity?

MR. BRYDEN: Let us assume for the sake of the dissussion that that fellow was the owner and he may have a mortgage on his property that he has brought down over the years to, say, 20 per cent. As it stands at the moment, if he is the seller, presumably he can, or his purchaser can, arrange a mortgage on 66-2/3. Now, it is possible that he may not have the additional down payment himself and then you get into the position where either the seller has to give back a second mortgage -- in other words, take a time payment on the equity -- or else he has to go in search of funds. As far as the seller is concerned, if we move into this other situation it struck me -- and maybe I am on a sticky wicket -- it struck me that there is a very large equity position existing in older houses, a large part of that, you might say, is on earned increment which has come from the exceptional spiral in houses to the extent that the savings he gets out of the sale are on balance kept in capital form, and then I think that is all right, but I could see situations where it would seem to me that a lot of people might very well -- and this is not the old people the Chairman

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was talking about -- but a lot of people might very well exchange for another new house and only put down the minimum equity and then proceed to have a windfall, if you will, of X thousands of dollars which they proceed to go around the world on, or something of that kind. That is what I mean by monetizing it. Is that a bad thing?

MR. RIEDER: I think it would be difficult here as you are talking to a group of life insurance people and this has not been a traditional mortgage field for life insurance companies, but is for other institutions like the trust companies, and so on.

THE CHAIRMAN: You will find there are very few institutions that are particularly interested in this for various reasons, I suppose.

COMMISSIONER LEMAN: What does this do to the development of towns?

MR. RIEDER: It lets the downtown go to seed.

MR. BRYDEN: I do not know that that is a valid comment on it. The F.H.A. has been available on existing houses in the United States for many years and I do not know that the central areas of their cities have held up any better than the central areas of ours because the F.H.A: have not been available on existing houses. Certainly we have been in most of the major cities in the United States and it is not our experience that the downtown areas are built up any better than ours.

THE CHAIRMAN: Is it not all a question of this: The people have an asset that is/not easy to sell.

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THE CHAIRMAN: Is it not all a question of [illegible] ople have an asset that is not easy to sell.

MR. BRYDEN: That is right.

THE CHAIRMAN: Because of the difficulty of finding a purchaser who has the cash?

MR. BRYDEN: That is right.

THE CHAIRMAN: And there are many people who would like to buy that class of a house and the seller either has to take a very much lower price than he would like to accept and which is out of line with -- if there is such a thing as a true value on a house. Somebody wants to sell it and somebody wants to buy it, and what is wrong with some agency making it possible by financing?

COMMISSIONER GIBSON: Do you gentlemen think there is a gap in the financial system?

MR. McCARTHY: There may be, sir, but I don't know that it has ever been demonstrated. I would venture the opinion that the people who talk about this are the minority and there is more noise than there is substance. I make that observation having in mind that the Commission has heard much about this across the country, and it was that I had in mind. The bulk of people buying houses today buy new houses and not old ones.

THE CHAIRMAN: You would be surprised how difficult it is to buy a new house in certain places.

COMMISSIONER BROWN: Is this because it is easier to buy a new house?

MR. McCARTHY: I think so, and I think people want new houses as compared to old houses.

THE CHAIRMAN: There is a tremendous demand for old houses in certain areas of Toronto. It is very difficult to find a house for sale. There doesn't seem to be any problem of financing. People, if necessary, will pay cash for it.

COMMISSIONER GIBSON: Could we change the subject a little and ask one or two questions about N.H.A. mortgages? What would you think of free N.H.A. mortgage interest rates?

MR. McCARTHY: Freeing them?

COMMISSIONER GIBSON: Yes, just having a market rate and not a fixed rate?

MR. McCARTHY: The posted rate under N.H.A.,

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I think, is an integral part of the system. To have a variation on it , it seems to me, we must develop a two-sided market -- a bid and ask market for N.H.A. mortgages where people trade at discounts or premiums as do the F.H.A. mortgages in the United States. We have a piece of that market -- Central Mortgage and Housing has periodically made mortgages available. We have not organized a two-sided market yet. I would venture the opinion it is a need that will only be filled when it can be done so profitably by some group. Who that group may be, or how they would go about it, I am not certain.

COMMISSIONER GIBSON: You don't think it would happen if the rate were free?

MR. McCARTHY: The rate would be, in effect, free if the two-sided market existed.

COMMISSIONER GIBSON: But you say it does not exist on one side, and if it were free would this speed the development of such a market?

MR. McCARTHY: We are still left with the question of who would be the group on the bid side.

COMMISSIONER BROWN: Presumably somebody would have to set the rate,anyway if it is going to be something that is guaranteed by the Federal Government?

Mr.McCARTHY: I think that is correct.

COMMISSIONER GIBSON: It is theoretically quite possible to have a guarantee at a set rate.

MR. McCARTHY: It may be.

MR. LEMMON: The rate set is not a fixed rate. It is a maximum rate. There is nothing to prevent

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[illegible] The rate set is not a fixed rate. It is a maximum rate. There is nothing to preven

lenders from making loans under that rate, and at certain times in the history it has been done. It has been the feeling of Central Mortgage and Housing, apparently, or some authorities in the government that if the rate was set free it would be automatically set higher than it should be, and I don't think that necessarily follows at all. I think the market conditions would set that rate the same as it sets the rate on corporation bonds or municipal bonds or conventional loans or anything else. The set rate on National Housing Act loans has been used as a method of influencing mortgage rates generally. If it were set free, that could not be done.

COMMISSIONER GIBSON: You don't see any particular objection to it?

MR. LEMMON: No. It would have the advantage of making the flow of funds in the N.H.A. loans much easier over the years. There have been periods when the flow has gone down because the rate has been not too attractive. As a matter of fact, there was a period when the flow of funds from private institutions practically disappeared. If the rate was permitted to be flexible such a situation would not occur.

COMMISSIONER GIBSON: Does the maximum loan provision under the N.H.A. affect the quality of housing, in your opinion -- that people will skimp to get under that maximum amount?

MR. LEMMON: That is a matter of opinion; it can only be a matter of opinion. In our judgment, I think the inspectors of C.M.H.C. have done a pretty

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good job across the country of protecting the purchasers against that sort of skimping. There certainly is a tremendous urge on the part of the builders to get under that maximum, and they undoubtedly would do such skimping if they could, but our own experience is that the inspectors of C.M.H.C. have done quite a job in preventing that sort of thing going on.

COMMISSIONER GIBSON: What about the pre-payment privilege of N.H.A. mortgages? Have you any views about that? Is it too liberal to make it an interesting investment?

MR. LEMMON: It certainly is one factor that the lenders take into account, that in periods of higher average interest rates you are never sure of the term of N.H.A. loans, and the witness of that is that we had discussions with Central Mortgage and Housing a few years ago and they finally agreed that N.H.A. loans on income properties could not be refunded within 10 years, and that made them much more attractive to institutional investors. Single houses are not quite so important because they don't tend to be refunded for a saving in interest to the same extent that income properties do. Generally speaking, when a man contracts a mortgage on his house he goes on until he sells it or until some other circumstance results in the repayment, but he does not do it to save one-half of one per cent in the interest rate. So, it is perhaps not so important with individual houses.

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COMMISSIONER BROWN: On that particular [illegible] there been any thought at any stage

of developing a mortgage document somewhat similar to that used by the building societies in the United Kingdom where the interest rate is subject to fluctuations?

MR. LEMMON: Not in this country, to my knowledge.

MR. BRYDEN: I don't think so.

MR. BROWN: Would it help at all?

MR. LEMMON: No, I don't think the situation is parallel at all. The biggest lenders on housing in Canada are life insurance companies with long-term liabilities who like to have their investments for relatively long terms. The Building Society on the other hand, has short-term liabilities and can change the rate of interest they pay on their deposits and on their shares, and therefore if the rate of interest on their assets goes down they can cut the rate of interest on their liabilities. Life insurance companies, on the other hand, cannot do that.

MR. BRYDEN: I think Mr. Westwater would agree that is one of the reasons why the United Kingdom companies tend not to have so many mortgages as we do -- the fact it is a pretty short-term investment over there.

MR. WESTWATER: This is so, yes.

COMMISSIONER GIBSON: On the question of interest rates -- and I am referring to conventional mortrgages -- when interest rates rise do you tend to take a little more generous view of the period of amortization -- the term of the loan?

MR. BRYDEN: That is a difficult one to answer. I would think probably no, because it is quite

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MR. BRYDEN: That is a difficult one to answer. I would think probably no, because it is quite

normal that you attempt to tie your amortization period to some life of the asset -- not the life exactly but the economic life of the asset, and I think that is the governing factor on most amortized amounts. So, I don't think you would alter it because you happen to have a change in the interest rates.

COMMISSIONER GIBSON: Do you tend to alter the size of the loan in making the conventional mortgage when interest rates rise or decline? In other words, if the rate is a little better do you have to be a little more generous in the amount of the loan, or vice versa?

MR. LEMMON: It might even work vice versa. In periods of tight money the borrower's bargaining power is not so good and he is more apt to accept the loan you offer. In periods of low interest rates the lender's bargaining power is not so good.

COMMISSIONER GIBSON: In periods of tight money you have got less to go around?

MR. LEMMON: Yes.

COMMISSIONER GIBSON: So you are trying to keep it less even though the interest rate is better?

MR. LEMMON: Yes.

THE CHAIRMAN: Gentlemen, the authorities have encouraged us to vacate this building by 4.15 P.M. We will now adjourn until 8.45 in the morning.

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Royal Commission
on
Banking and Finance

The Canadian Life Insurance Officers
Association (concluded)

Hearings
held at
Ottawa

Vol.	Date.
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Toronto, Ont.

ROYAL COMMISSION ON BANKING

AND FINANCE

Hearings held at Ottawa,
Ontario, on Tuesday,
July 10th, 1962.

THE COMMISSION

The Honourable Dana Harris Porter
Chief Justice of Ontario
Toronto, Ontario - Chairman

Mr. W. Thomas Brown, M.B.E.
Investment Dealer
Vancouver, British Columbia

Mr. James Douglas Gibson, O.B.E.
Banker
Toronto, Ontario

Mr. Gordon L. Harrold
Agriculturalist
Calgary, Alberta

Mr. Paul H. Leman
Corporation Executive
Montreal, Quebec

Mr. John C. MacKeen
Corporation Executive
Halifax, Nova Scotia

Dr. W. A. Mackintosh
Vice-Chancellor
Queen's University
Kingston, Ontario

Mr. H. A. Hampson - Secretary

Mr. Gilles Mercure - Joint Secretary

Ottawa, Ontario,
Tuesday, July 10th, 1962.

--- At 8.45 A.M. the hearing commenced.

THE CHAIRMAN: Call the meeting to order.

COMMISSIONER GIBSON: Mr. Chairman, we were asking a few questions when we adjourned yesterday afternoon about the mortgage end of the business and I would like to pursue this a little further. One question that was discussed is the same question Mr. McCarthy said a few words about, how funds are moved from one type of investment program to another. I would like to follow this up a little further. Suppose you have a given amount of funds or an estimated amount of funds which you are going to have available in the coming year, or whatever coming period we are looking at, what are the considerations that determine the proportion of those funds that will go into mortgages? I realize you may shift from one to another as things go along, but when you are starting out on the year, how do you say, well, how much of this will go into mortgages?

MR. McCARTHY: Well, I suppose we would begin by making a judgment as to whether or not we want to increase the proportion of funds for new mortgages or whether we want to hold that proportion constant. To hold a mortgage portfolio constant a mature mortgage portfolio requires to hold the returns that are coming along.

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into account the needs of keeping a mortgage program together. This requires a certain minimum amount of business flowing through it in the course of a year. Beyond that it is a case of the relative attractiveness of mortgage rates as you look ahead against other forms of rates.

COMMISSIONER GIBSON: You look at the relative differences in yield between mortgages and other types of investments and this provides a basis of whether you increase or decrease your mortgage program but you have to take a certain volume a year to keep the machinery turning over.

MR. McCARTHY: It would be my opinion that the mortgage instrument would have to be extremely unattractive versus other investment criteria to turn the program off completely.

COMMISSIONER GIBSON: When your other yields are somewhat more attractive and there is a change in favour of other types of investments would you be inclined to lower your standards in the mortgage area a bit in order to get the better yield? There is a suggestion in your brief that there is a variation of one-quarter of one per cent between the first class mortgage and the fairly good one. That seems like a rather small variation to me. Do you go out of that range any further in order to keep your yield up?

MR. McCARTHY: In my own experience no, but others may wish to comment on that.

MR. FALKNER: I do not think that it is a question of diluting the quality of the investment.

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MR. McCARTHY: In my own experience no, but others may wish to comment on that.

MR. FALKNER: I do not think that it is a question of diluting the quality of the investment.

Some mortgages may command a rate of 6-3/4 per cent and by the same token it would be perfectly logical to make another mortgage investment on a different type of property possibly at 6½ per cent. I am simply using these percentages as an example.

COMMISSIONER GIBSON: Well, sticking to the residential mortgages there is a difference in quality here. For instance, yesterday we were talking about mortgages on existing properties and here is an area where perhaps you get a little higher rate.

MR. FALKNER: It might appear logical that that would be so, but I think the risk might be reflected possibly in underwriting practices and it should command the same rate of return as on an old residential property as possibly a new property and the quality of the investment might be reflected in the ratio of the loan you would be prepared to make.

COMMISSIONER MacKEEN: Would not location have a good deal to do with it?

MR. FALKNER: Very definitely.

MR. RIEDER: I believe there is one further factor in planning your program for the year -- your demand or probable demand for housing in the coming year.

COMMISSIONER GIBSON: You look at the supply that is likely to be available?

MR. RIEDER: The need and the supply.

COMMISSIONER GIBSON: Does the mortgage program vary quite widely in individual companies?

Your total figures do not vary so very widely but is there a big variation in individual companies from year to year?

MR. McCARTHY: Some companies are more flexible than others, I believe. There are some companies who use the mortgage investment field as the principal and almost the main outlet for most of their funds and there are other companies at the other extreme that will vary a program as much as 50 per cent from year to year depending on their assessment of the relative attractiveness of mortgage development.

COMMISSIONER GIBSON: The more attractive it is the more likely it is to be fairly steady?

MR. McCARTHY: No, I would not say that. It is just what is in the minds of the people who determine this and that I do not know.

MR. LEMMON: It may be interesting for you to note the cases in the last five years and the variations between the high mortgage loan approvals and the low mortgage loan approvals would be of the order of 30 per cent; in other words, the low order would be about 70 per cent of the high order.

MR. POYNTZ: Our own has varied more than that -- as much as double in one year what it was the year before.

COMMISSIONER GIBSON: Are these decisions made at the beginning of each year?

MR. POYNTZ: Yes they are.

[illegible]

year to year?

MR. McCARTHY: Some companies are more flexible than others, I believe. There are some companies who use the mortgage investment field as the principal and almost the main outlet for most of their funds and there are other companies at the other extreme that will vary a program as much as 50 per cent from year to year depending on their assessment of the relative attractiveness of mortgage development.

COMMISSIONER GIBSON: [illegible] it is the more likely it is to be fairly steady?

MR. McCARTHY: No, I would not say that. It is just what is in the minds of the people who determine this and that I do not know.

MR. LEMMON: It may be interesting for you to note the cases in the last five years and the variations between the high mortgage loan approvals and the low mortgage loan approvals would be of the order of 30 per cent; in other words, the low order would be about 70 per cent of the high order.

MR. POYNTZ: Our own has varied more than that -- as much as double in one year what it was the year before.

COMMISSIONER GIBSON: Are these decisions made at the beginning of each year?

MR. POYNTZ: Yes they are.

MR. BRYDEN: In our case, Mr. Chairman, we normally reinvest the maturing section of the existing account and, of course, we are able with the big demand for houses in some years to run as high as more than 100 per cent of our total new money into the mortgage account, and this was reduced to a place some ten years ago where we were putting about 50 per cent of our new money in. That was raising the percentage of new and for the last three or four years our ratio has remained relatively constant at around 38 per cent and 40 per cent with the result that you are reinvesting your repayments at about 38 to 40 per cent of your new payments into that area. There may have been in the last year or so a tendency for the total to decline slightly but not much.

COMMISSIONER GIBSON: Mortgages have to become relatively more attractive in relation to bond investments because of the reduction in the cost of administration. There is quite a marked reduction in the cost of administration.

MR. BRYDEN: There has been quite a reduction, yes, over a time but probably the answer to that is that your existing organizations have been able to get a bigger volume with very little increase in personnel and other costs.

If I may, Mr. Chairman, the subject came up about loans on existing houses and we have found amongst our papers that the insurance companies -- and this was a percentage based on their total loans -- the new

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residential loans in 1961 were 67 per cent of all loans, loans on existing residential were 14 per cent which gave you a total of residential loaning of 81 per cent. Then new other urban would be 14 per cent, existing other urban 5 per cent, and farm is nothing, so the other urban would be 19 per cent.

COMMISSIONER BROWN: What is "other urban"?

MR. BRYDEN: That would be office buildings, factories, and anything other than residential -- stores, shopping centres, et cetera.

COMMISSIONER BROWN: Commercial and industrial?

MR. BRYDEN: Commercial and industrial et cetera. And that has changed relatively little over the last three years. The existing residential loans as a percentage of total loanings in 1959 was 16 per cent, in 1960 was 12 per cent, in 1961 14 per cent. So that is the extent to which the insurance industry participated in loans on existing houses as of now.

COMMISSIONER GIBSON: That is as of 1961, is it?

MR. BRYDEN: The last three years, 1959, 1960 and 1961.

COMMISSIONER GIBSON: Thank you very much. Going back to the decline in administrative costs you say it is largely a case of bigger volume, is it?

MR. BRYDEN: I would have thought so.

MR. LEMMON: Yes, almost entirely. The absolute expenses have gone up but it is the base that has increased much faster.

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MR. LEMMON: Yes, almost entirely. The absolute expenses have gone up but it is the base that has increased much faster.

COMMISSIONER GIBSON: And this would apply more to larger organizations than to smaller ones?

MR. LEMMON: I presume it would.

MR. HOLMES: Mortgage accounting is another factor in cost. They have been able to get mortgage accounting effectively onto the machines which is much faster than formerly.

MR. POYNTZ: I think the relative mix has something to do with it all. If the mortgage account is being held fairly stable by the reinvestment of repayments only the acquisition cost is relatively lower.

COMMISSIONER GIBSON: Could you give us some idea of the differences in costs of various kinds of residential mortgage loans? First of all, is there any substantial difference in cost between getting National Housing Act mortgages and conventional mortgages of approximately the same size?

MR. LEMMON: We have tried in our shop, Mr. Chairman, to put some figures on this. It is awfully difficult, it is a pretty arbitrary procedure but generally speaking it is more expensive to put a National Housing Act loan on your books than a conventional loan. There is another party involved and there are certain procedures to be gone through and certain approvals to be obtained, certain regulations to be followed which introduces another factor and principally because there is a third party in the transaction the cost of putting a new National Housing Act loan on your books is more than putting a small

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conventional loan on your books. The exact extent of that would be a pretty arbitrary estimate.

Mr. Rieder brings up the question that there are two ways of handling National Housing Act loans. You can do it on insured advances or uninsured advances. In the case of uninsured advances the lender gets part of the fee that C.M.H.C. charges for the National Housing Act loan to offset the expense that the lender incurs in doing the inspections and following it through. That increases the expense and also the lender gets some fee for doing it. In the insured advances the lender is not put to the same extra expense because C.M.H.C. carries the risk over the construction period.

COMMISSIONER GIBSON: Which of those choices do the insurance companies tend to prefer?

MR. LEMMON: I think each company will have to speak for itself on that one. In our case we are operating an existing organization with an experienced manager and inspectors and we tend to proceed on what we call the uninsured advance basis. In other areas where we do not have such an organization we operate on the insured advance system.

MR. RIEDER: We are the same.

MR. FALKNER: We are substantially uninsured lenders across the country.

COMMISSIONER GIBSON: Is this difference in costs between N.H.A. and conventional an important factor in the decision on how much of these various kinds of mortgages you have on your books?

MR. LEMMON: There again, Mr. Chairman, the decision would be different from company to company. I am only speaking of our own experience where it is a factor; in other words, where the rate spread gets to be down to one-quarter of one per cent between conventional and National Housing Act you might put one product mix on your books; if it got as wide as one-half we would probably reduce our participation in the National Housing Act and steer more to conventional and the excess cost of the National Housing Act is a factor in it -- not the final determining factor because, like most companies, we have an existing organization and it does not save us any money to have that organization sitting on its hands.

COMMISSIONER GIBSON: Now, on the differences in costs of putting mortgages into companies' books, does it cost more for different sized loans, say, between $10,000 and $20,000 on a single unit structure?

MR. LEMMON: Well, many of the costs are similar, if not the same, regardless of the size of the loan, and therefore on a unit basis, on a dollar invested basis the cost of the larger loan is less than the cost of the smaller loan.

Generally speaking we use a little more inspection the larger the loan gets, but the costs do not go up in relation to the size of the loan.

COMMISSIONER GIBSON: Is that one of the reasons why some companies seem to prefer conventional organization because the average size is a little larger than National Housing Act?

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COMMISSIONER GIBSON: Is that one of the reasons why some companies seem to prefer conventional organization because the average size is a little larger than National Housing Act?

MR. LEMMON: Some companies carry them to a very extensive degree and they are only interested in very large loans from a cost factor.

COMMISSIONER GIBSON: I am talking of residential loans now. But there is a difference between a $10,000 mortgage and a $20,000 mortgage, the cost of putting it on your books would not be very great, I suppose?

MR. LEMMON: No, it would not, but the spread is not usually that wide. The National Housing Act loans go up to $14,000 now. It is true that conventional loans go to $20,000, $25,000, but an awful lot of them are in the area of $15,000 or $20,000 anyway, so that the difference in size as far as single houses are concerned,I do not think, is nearly as great a factor as the difference in absolute rate between National Housing Act and conventional.

MR. BRYDEN: I was going to say, still in the area of housing, once you move over into apartments it is obviously cheaper to administer one apartment loan for, say, $500,000 than a number of single unit loans of $10,000 or $20,000. It is cheaper to administer and acquire.

COMMISSIONER GIBSON: What about the difference in costs between a mortgage on a new residence or new residential property that is being built and an existing property, is this a factor?

MR. LEMMON: In my opinion, no.

MR. BRYDEN: You go through the same valuation procedures, the same procedure of putting the mortgage in

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MR. LEMMON: Investigation of credit, et cetera. I do not think that is an appreciable factor.

COMMISSIONER GIBSON: If there was a mortgage already on an existing property and it was just a matter of increasing it, this would reduce the cost slightly?

MR. LEMMON: Yes, it is the legal costs it reduces to a considerable degree.

COMMISSIONER GIBSON: When mortgage money is available do residential borrowers show so much response to changes in interest rates in your view? In other words, are people less apt to take on the business of buying a house if the interest rate is one per cent higher than if it was a bit lower?

MR. LEMMON: I am afraid that as in the case of small loans and instalment finance that interest rate is only an incidental factor in that. It becomes a factor if two houses are for sale and one carries a $6\frac{1}{2}$ per cent loan and the other carries a 7 per cent loan. It may get to be a factor in the relative attractiveness of those two houses. But in my opinion the fact that an interest rate is 7 per cent or $6\frac{1}{2}$ per cent is not a factor in whether he buys a house or not.

MR. BRYDEN: I think normally, Mr. Chairman, the mortgage loan calling for a monthly payment, it is the amount of the monthly payment that he ties into his own budget. I do not think the interest rate has a very great influence in that case.

COMMISSIONER GIBSON: Of course the monthly payment is affected by the interested rate?

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MR. BRYDEN: Oh, sure it is but I think the normal buyer looks at the amount of money it is going to take him to carry that loan per month, interest and principal and that is reflected in his own budget.

COMMISSIONER GIBSON: You do not think he is particularly sensitive to moderate changes in these actual charges?

MR. LEMMON: There are two other factors in the actual charge zone. One is the size of the loan and the other the term of the mortgage and if you juggle either two factors then the interest can fade out actually as a factor.

COMMISSIONER BROWN: This came up yesterday as to the extent you did juggle mortgages. I think the answer was you did not juggle mortgages.

MR. BRYDEN: I think that is a reasonable answer to that one. What I had in mind more particularly was when the National Housing Act extended its terms of mortgage from 25 to 30 years a number of us had builders' loans on our books that were unsold, but there is a certain requirement as far as adequacy of carrying charges on a house to the man's income.

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There was some juggling of the term of the loans to enable those houses to be sold. I do not think, if that answer which was made yesterday is true, that that is an extensive practice on the part of lending institutions because if the borrower is in the position where you have to extend the term of the loan for two, three, four, five years and there is not the income to qualify it, he is a pretty marginal borrower and you try to find somebody else or let the loan go.

COMMISSIONER GIBSON: Would the individuals that build and own apartment houses be more sensitive to interest rate changes than ordinary residential purchasers?

MR. LEMMON: I think that is a fair statement. I would say they are more sensitive.

COMMISSIONER GIBSON: When interest rates go down, this tends to bring in more applications of this kind, does it?

MR. LEMMON: I would not have thought of it in those terms. I think the apartment situation is more the determining factor as to whether there is a large volume of applications come in or not. I do not think the interest rate is the determining factor. I was thinking more in my answer that if a man is planning an apartment house and it looks as if he is going to be able to get a loan at 6½per cent but before he gets finished with his plan he finds that it is 7 per cent, he may take another look at it.

COMMISSIONER GIBSON: So there would be quite a few pieces of postponements when the rates were rising?

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COMMISSIONER GIBSON: So there would be quite a few pieces of postponements when the rates were rising.

MR. LEMMON: In our case, yes. He assesses his market and he decides he can get $125 or $135 per month for those suites, he looks at the economics of it and finds there is only one-half of one per cent going into the interest rate; that makes him think about the economics of it.

COMMISSIONER GIBSON: So he responds properly, as he should. What about the other side of it? This same man has postponed this project because the rate has gone up more than he expected in his plans and there is not a margin there. Does he wait until the rates go down again and then take out the plans and dust them off?

MR. LEMMON: He certainly takes them out and dusts them off and if the market for apartments is still the same as it was before he may proceed with it.

COMMISSIONER GIBSON: So it would work to some extent both ways?

THE CHAIRMAN: Providing the cost of construction has not changed.

MR. LEMMON: He would then determine the market, and if the other factors have not changed he may then proceed.

COMMISSIONER GIBSON: Let us say that the other things are equal.

MR. LEMMON: All things being equal, yes, that is right.

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questions I should like to ask in connection with mortgages.

Do the different provincial laws affect your distribution of mortgage funds at all? We have heard stories in the different provinces, that it is a little more difficult to make your mortgage effective.

MR. LEMMON: The provincial legislation does vary from province to province, and the attitude of the courts varies from province to province. I cannot help but think it does have some effect on the lender's attitude. Just how much effect is awfully difficult to measure.

COMMISSIONER BROWN: Does it affect your thinking on distribution of funds?

MR. LEMMON: I cannot help but think it does, but to what extent I cannot tell you. We ourselves make loans in all provinces. I think our committee does bear in the mind the fact that the situation is different from province to province.

COMMISSIONER BROWN: The other question I have to ask is somewhat along the same lines. Mention was made of the fact that locality enters into the question of rates to a certain degree.

MR. LEMMON: Yes.

COMMISSIONER BROWN: This would be locality referring to being near a city or out in the country, presumably; in a good area or poor area?

MR. LEMMON: You could take extreme cases, Mr. Chairman. Certainly the rate of interest in the mining communities in Northern Ontario are higher than

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those in the more desirable residential areas in Toronto.

COMMISSIONER BROWN: Yes. My question now is directed to a wider scale. Are there large regional differences in interest rates? For instance, are your mortgages rates higher in the Maritimes and in the West than in Ontario?

MR. LEMMON: Mr. Chairman, that is a peculiarity of mortgage financing in Canada. There is much more uniformity of rate on mortgage lending across Canada than there is across the United States. There is much more variation in the rate between communities in the United States than there is between communities in Canada. Generally speaking in a desirable residential area in Vancouver, Winnipeg, Ottawa, Montreal or Halifax the rate would be about the same.

COMMISSIONER BROWN: One is tempted to ask if you deliberately left out reference to Toronto.

MR. LEMMON: No, I brought Toronto into the picture before and I saw some smiles go around so I left Toronto this time.

That is not necessarily the case in the United States. For instance, on the Pacific Coast of the United States; Los Angeles, San Francisco, the rates are possibly higher than they are in Philadelphia, Boston and New York.

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COMMISSIONER BROWN: Would you care to make a comment as to this being because of the different structure of the mortgage industry in Canada than in the United States?

MR. LEMMON: The reason for it can only be a matter of opinion. It cannot be a categorical answer.

Part of the reason is that the lenders in Canada tend to be national lenders lending from Halifax to Vancouver. In the United States the lenders are much more local lenders than they are in Canada. Los Angeles for instance, being an area of tremendous growth with wide demand for money and the local money not meeting it, it takes a little more in attraction to overcome the inertia in persuading lenders from Boston institutions to lend in Los Angeles than it does in Canada where the lenders are generally national lenders.

COMMISSIONER LEMAN: Is there really more supply in the United States in relation to the demand for mortgage loans which would make the market a little more sensitive there?

MR. LEMMON: Certainly the United States is more of a capital producing country than Canada, although I still think the other factor is by far the more important factor than the relative supply and demand for funds in the two countries.

COMMISSIONER GIBSON: Talking about the comparative situation in Canada and the United States, I was wondering if Mr. Falkner might like to say a word or two about his view of Fanny Mae and its effect in producing a mortgage market in the United States?

MR. FALKNER: I will offer what I can, Mr. Chairman.

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MR. FALKNER: I will answer that first, Mr. Chairman.

You will appreciate that while I represent the American company, I represent that portion that

operates exclusively in Canada. Fanny Mae was developed in the United States -- what is called Fanny Mae is the Federal National Mortgage Association -- I believe in 1938 and one of its functions was to generate what they called a secondary market. That is, it was a governmental vehicle set up to buy and sell ensured F.H.A. loans which in essence compare with our N.H.A. ensured loans, or Guaranteed Veterans' Administration Loans. This was a government sponsored loan which was 75 per cent ensured and 25 per cent conventional. Fanny Mae in the open market bought and sold these types of loans.

As a matter of interest, I spoke to our people only this morning to get further details on its operation, and I am told that it is not very effective today.

It buys mortgages when rates are declining, and usually buys them at a discount, and it sells mortgages in times of rising rates. Not all companies participate. Usually the major buyers would be those companies that have not got an organization to put mortgage loans on their books. The sellers might be insurance companies and banks.

I think that possibly its role has probably been exaggerated; it has probably been exaggerated. This is the impression that I got today in respect to it.

One feature about it that prohibits, or at least keeps a number of participants out is the fact you must subscribe to the stock of Fanny Mae to the extent of 2½ per cent of the volume of loans that

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you sell, and you then become a shareholder in Fanny Mae. I believe this stock over the years has paid a dividend averaging somewhere in the area of 5 to 5¼ per cent. A lot of companies objected to that feature in Fanny Mae. I believe that the purpose of that is to ultimately wind up creating a company without any government ownership.

That would encompass my knowledge of Fanny Mae, Mr. Chairman.

COMMISSIONER GIBSON: You say it sells when rates are rising? Surely that would be the other way around?

MR. FALKNER: I am sorry, when prices are rising.

COMMISSIONER GIBSON: When prices are rising, yes. It deliberately tries to stabilize the market?

MR. FALKNER: Yes, that is correct.

COMMISSIONER GIBSON: But you are not too impressed with its record in stabilizing the mortgage market?

MR. FALNER: I do not think so. There might be representatives of companies here who operate both in Canada and in the United States from their Canadian headquarters who might have more experience than I in this regard, but this is the impression I gained of the operation of Fanny Mae.

COMMISSIONER GIBSON: Is it a useful adjunct to the insurance company from the liquidity point of view in providing a place where you can go and sell a large batch of mortgages?

(Page 2536 follows)

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MR. FALKNER: I suppose if you got over invested in mortgages it would probably fulfill some use there.

MR. BRYDEN: Mr. Holmes, would you care to make any comment in respect to that operation?

MR. HOLMES: We have not had nay operation in respect to F.H.A. loans at all.

MR. BRYDEN: Mr. Chairman, I wonder if in respect to the matter of the secondary mortgage market, I could refer your research staff to a book called The Secondary Mortgage Market, Its Purposes, Performance, and Potential by Oliver Jones and Leo Grebley, a publication of the Real Estate Research Programme, Graduate School of Business Administration, University of California. It deals in great detail with the development of the secondary mortgage market in the United States.

THE CHAIRMAN: That is published by the University of California?

MR. BRYDEN: Yes.

COMMISSIONER GIBSON: I think we have that, Mr. Bryden.

THE CHAIRMAN: Apparently we have it.

MR. LEMMON: It is the best book we have on that subject.

MR. BRYDEN: Mr. Gibson, I referred it to your research staff.

THE CHAIRMAN: They have it.

COMMISSIONER GIBSON: Thank you very much.

THE CHAIRMAN: It has not reached us yet.

MR. BRYDEN: I see.

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COMMISSIONER BROWN: I wonder if we could

switch now from mortgages back to a subject we thrashed around a little bit yesterday, and that is the knotty problem of the common stock portfolio.

First of all we would just like to clarify the situation with respect to the present legislation and the 15 per cent rule. The points that arise are first, that a United Kingdom company operating in Canada show assets each year at the market value. What happens if your stock holdings, because of a market increase, show that you are in excess of that 15 per cent?

MR. WESTWATER: You are required to make up the deficiency in your deposit with bonds or mortgage investment, or some other mediary of investment until such time as the whole deposit grows in size to the 15 per cent common stock. You cannot put any more common stock up until the delivery has been restored.

COMMISSIONER BROWN; This applies even though the market value of your other securities has not gone down and in fact your surplus has been increased by an increase in the market price of your common stock?

MR. WESTWATER: That is so.

COMMISSIONER BROWN: What happens with a Canadian company? We have this list that you made up showing the four columns that we discussed yesterday, and you have the book value and the market value. What happens if the book value of the common stock is only 5 per cent and the market value goes up to say 16 per cent?

MR. LEMMON: The Canadian Act says this is based on book value so nothing happens.

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MR. LEMMON: The Canadian Act says this [illegible]

COMMISSIONER BROWN: Nothing happens even though the market value has increased. You take a look at the whole thing to see that you are in good standing?

MR. LEMMON: That is quite right because the wording of the Act is that 5 per cent of the ledger value, or 10 per cent in the case of real estate is the figure.

COMMISSIONER BROWN: I see.

MR. LEMMON: It is based on ledger value.

COMMISSIONER BROWN: This means that the United Kingdom companies operating in Canada are under greater disabilities in respect to this problem of market fluctuation and its effect on the common stock portfolio?

MR. LEMMON: That is right.

COMMISSIONER BROWN: But they are prepared to operate much nearer this limit than Canadian companies. Why are Canadian companies so reluctant to move up?

MR. BRYDEN: Once again, Mr. Brown, I think we are getting back to the matter of the valuation procedures that we have and the effect that a downward swing in a large sized stock portfolio, would have on your surplus. I think those two things are tied up together. If, for example, the average surplus position say of the Canadian companies was 5 per cent, and if you had a common stock portfolio of 15 per cent, and if you had a 1/3 decline, as conceivably you might have at some point; if that happened to be on your valuation date your balance sheet effectively would show

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your surplus wiped out.

COMMISSIONER BROWN: The common stock holdings of the Canadian companies, you say, on the average are shown at only about one-half their market value, so they have this margin in there already, have they not?

MR. BRYDEN: Yes, but the effect that a large swing of common stock market values could have on your surplus I think is one of the reasons why the Canadian companies do not approach the 15 per cent limit, and why you would find that the common stock holdings are a much smaller percentage. I think they are $3\frac{1}{2}$ to 4 per cent even at book value.

COMMISSIONER BROWN: The United Kingdom companies are subject to much greater fluctuations than Canadian companies?

MR. LEMMON: Only in one small piece of their business. Namely, the Canadian piece which may be only 10 per cent of their total operation.

MR. POYNTZ: As we mentioned yesterday, there is some flexibility in the valuations of the liability supply.

COMMISSIONER BROWN: But not for Canadian companies.

MR. POYNTZ: But not for Canadian companies.

MR. LEMMON: That is only a small percentage of their total operation whereas in respect to Canadian life companies, it is our whole operation we are talking about.

COMMISSIONER GIBSON: How could that explain

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COMMISSIONER GLESON: How could that explain

the present low ratio, because there is a sizeable margin between the book and market, and in addition the average ratio is only 3 per cent? In these circumstances supposing Canadian companies were to double their holdings of stock, and perhaps even more than that; that still would not affect the surplus very much, would it?

MR. RIEDER: Most of our portfolios were acquired some years ago when stock prices were low.

COMMISSIONER GIBSON: But they went down recently, Mr. Rieder.

MR. RIEDER: Not far enough, perhaps.

COMMISSIONER BROWN: The point is, if they were acquired a long time ago and show on the books at 3 per cent and the market is double that, you could see the market cut in half and your present holdings are not going to affect your surplus position.

MR. HOLMES: If you had 15 per cent it would cost quite a bit to write it down to half. If we went up to our limit at half we would have 30 per cent at market value of common stock and 15 per cent at book. That would be quite a charge on surplus to get it down to half; that is your book value down to half of your market, unless you happened to buy at the right time and have the appreciation.

COMMISSIONER GIBSON: We are not really saying it should be at 15 per cent or anything else. We just wondered why it is not higher than 3, because it is hard to see that this is much of a barrier under the present situation.

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COMMISSIONER BROWN: Under the circumstances, why do you want it up to 25 per cent?

THE CHAIRMAN: I understood they were not too enthusiastic; I understood that from what you said yesterday.

MR. LEMMON: Mr. Chairman, you are into the area here of different management operations of the various life companies, and it is quite true to say that the average of all life insurance companies is around three to four per cent. The average, as in most cases, covers a pretty wide variation. There are some companies who do not go into common stocks to any extent at all and have very negligible percentages; there are those who enter into it to a very heavier extent than the average would indicate.

Now, I would not want the Commission to get the impression that the industry operates as an average; it operates as a whole group of individuals. What will affect the one company's judgment is not the same set of factors that will affect the others. The valuation is one factor that enters into the management's approach on all the percentages of trade assets owned in common stocks. There are many other factors that would enter into that, and in some companies these factors directly eliminate common stocks from the program. One of the largest United States companies believes that common stocks does not constitute a suitable investment for life insurance funds at all and have publicly taken that attitude.

So that you are covering the whole wide range, and you may have companies at the upper end of that range

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who feel the limit over the years should be higher than 15 per cent, and at the lower end they could not care less.

COMMISSIONER BROWN: In other words, this is a minority report asking for an increase of 25 per cent?

MR. LEMMON: It is not a unanimous report asking for 25 per cent, but the ones who do not want it obviously are not opposing it.

THE CHAIRMAN: There may be some companies that are already approaching 15 per cent?

MR. LEMMON: I think the only ones that are really pressing on 15 per cent are the British companies. There are Canadian companies in the area of 10 per cent and 12 per cent, in that area. I do not think there are any actually pressing on 15; am I right in that?

MR. TUCK: Yes.

THE CHAIRMAN: I was wondering, and Mr. Brown brought this point out yesterday, I think. You look at the reserve requirements; I find that the brief does not deal with it as fully as it is dealt with in this little book which I was given yesterday entitled "Canadian Life Insurance Facts 1961". At the end of 1960 policy reserves equalled 78.8 per cent of the total assets of Canadian companies and other obligations to the policyholders, such as amounts left on deposit of interest and policy dividends payable accounted for 11.7 per cent of all assets.

Then, special reserves set up. As I see it from this book, at the end of 1960, the life companies

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Then, special reserves set up. As I see it from this book, at the end of 1960, the life companies

held policy reserves in Canada of $6 billion. Now that, as I understand it -- and if I am wrong I can be corrected on this -- that $6 billion is the reserve required by law. Am I right?

MR. BRYDEN: Fundamentally.

THE CHAIRMAN: So that the assets that they have in excess of that are -- I think the total assets are about $8 billion.

MR. BRYDEN: That is right.

THE CHAIRMAN: So that there is approximately $2 billion excess assets over the legal reserve.

MR. POYNTZ: The other liabilities are actual liabilities, Mr. Chairman; the policy reserves themselves are not a full measure of liability.

THE CHAIRMAN: Oh no, I understand that, but with that $6 billion reserve you are complying with the law?

MR. POYNTZ: In case you refer to other deposits, as for example dividends left on deposit, they constitute a liability just the same as the reserves on the policies. I think the $6 billion you spoke of is the actuarial measure of liabilities under policies, but the reserve is required also in respect of these other amounts.

THE CHAIRMAN: Well, what are they called? Are they the special reserves? Special reserves are mentioned here. What are they?

MR. BRYDEN: Could you tell us what page this is?

THE CHAIRMAN: It is on page 22, and I am looking

at this book. I do not know where to find it in the brief. I just cannot be clear on what the various things indicate and what it all adds up to and what the net position is.

MR. BRYDEN: Well, again reading from this, the policy reserve equals 78.8 per cent; that is the reserve which must be maintained by law as being the amount now which together with future premiums and future interest earnings will let you meet your commitments under your business in force.

In addition to that there are all sorts of current, very real liabilities; for example, amounts left on deposit, and so on. Now, these other obligations to policyholders, policy dividends and the amounts left on deposit, and so on, of the total are about 11.7 per cent of all the assets. Special reserves, liabilities and unassigned businesses in the paid up capital make up the remaining 9½ per cent.

On the next page, Mr. Chairman, page 23, the last sentence in the second paragraph speaks of, "In the case of Canadian companies surplus funds and contingency reserves", and that could be an investment reserve or a reserve for contingencies which equals 8 per cent of the assets at the end of 1960. And so really 92 per cent of the assets represents liabilities to policyholders either in reserve form being held or else actually payable. Does that clear up the point?

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THE CHAIRMAN: Well, 92 per cent is required?

MR. LEMMON: Yes.

THE CHAIRMAN: And that is in a sense ---

MR. BRYDEN: That is the margin, but not specifically allocated for some reason.

THE CHAIRMAN: But it is a surplus?

MR. BRYDEN: It is a surplus.

THE CHAIRMAN: And as far as that surplus is concerned, would it make any difference from the point of view of protection to the policyholders?

MR. BRYDEN: It is all for the additional protection of -- it is all for additional protection, but not needed.

MR. LEMMON: As Mr. Holmes pointed out yesterday, if one company due to its common stock values had that surplus cut in half or less, its competitors would lose no time in pointing it out to the general public that this particular company had played high, wide and handsome with policyholders' funds.

MR. HOLMES: The amendment to the Act to allow for mutualization -- the theory which Mr. McGregor followed roughly was this, that you could buy stock as long as at the end of a year that you bought stock -- at the beginning of the year you were to buy such stock during that year which would leave you with a 6 per cent surplus. That is the general theory of the way the Act is drawn up.

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THE CHAIRMAN: Yes. Well, what I had in mind was would it make any difference what that surplus is used for? Could there be any restriction on the type of investment which might be made?

MR. BRYDEN: The surplus ---

THE CHAIRMAN: It may not look like a very large surplus at the moment compared with the whole picture, but some day it may increase and with some companies it may be greater than with others, I suppose, is that so?

MR. LEMMON: Yes, although the variation is not all that wide. You see, we are participating companies mostly and tend to put out as policyholders' dividends everything over and above everything that is required as surplus.

MR. BRYDEN: I think normally at the end of each year you come up with what you might call a net operating revenue which really can represent an addition to your surplus funds. Now, normally out of that come your participating dividends and you would be inclined to pay out as big a proportion of those annual surplus earnings -- if you will -- in your dividends, but alternatively you would tend to hold back enough to keep your surplus gradually growing in line with the growth in the increase in assets.

THE CHAIRMAN: But not allowed to get beyond a certain reasonable proportion?

MR. LEMMON: Competition will prevent that.

MR. POYNTZ: Growing, but possibly not as

a ratio.

MR. RIEDER: The 8 per cent figure does not seem too much when you consider that an open portfolio can drop five points.

THE CHAIRMAN: You are not in the trust business, in other words.

MR. LEMMON: We are fundamentally insurance companies.

THE CHAIRMAN: And the moneys could be used.

MR. LEMMON: The agency department continually reminds us of that.

THE CHAIRMAN: And any surplus to be distributed?

MR. LEMMON: Yes.

COMMISSIONER MacKEEN: This might be an appropriate time to ask a question that has been intriguing me for many months. When we were going across the country it was seriously suggested, and in fact, it was recommended -- that consideration be given to not restricting reserves and various other moneys but requiring that they base at least 10 per cent of their reserves -- which would apply to banks, trust companies, life insurance companies and loan and savings companies -- in risk equities for more or less promotional enterprises, due to the developing sections of the country where there is a lack of capital for such a purpose.

What would your opinion be of such a recommendation?

MR. BRYDEN: Mr. McCarthy, I think that is one

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What would your opinion be of such a recommendation?

MR. BRYDEN: Mr. McCarthy, I think that is one

of the things you have had under consideration.

MR. McCARTHY: This business of financing new, untried enterprise?

MR. BRYDEN: Pardon?

MR. McCARTHY: This business of financing new, untried enterprises, new ideas? This has been one that has intrigued a number of the life companies for some period of time in the past year or thereabouts and the member companies, along with other financial institutions, including some of our banks, have been working towards the creation of a jointly owned risk enterprise capital type of undertaking, and we are approaching the point where I think this company will be formally launched with that very object in mind. The feeling is that this can be best undertaken by the companies generally rather than each of them attempting to do the job in its own investment department.

MR. BRYDEN: I believe the British practice is ---

MR. McCARTHY: Yes, there is the British example; the I.C.F.C. which was set up in the early postwar period by the banks there, and more recently -- I cannot recall the name offhand, but it is -- it is the Technical Development Corporation, which was set up largely with insurance company participation for the same purpose and a number of the Canadian companies who are doing business in England are shareholders in that company, and we think it is a thing that could be explored.

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some of us at least have tended to come to the conclusion that in creating new enterprise in Canada, the provision of finance is only one aspect of the problem; no amount of financial provision can create the administration or the skills that are necessary to create new businesses, and this is a problem that accompanies this and we will have to deal with it. It is just a question of when.

THE CHAIRMAN: I suppose the other advantage from the insurance companies' point of view would be that if the company lost money it would appear in a reduction of the surplus of all companies and not merely one.

MR. BRYDEN: It gives for each individual company a spread of risk, which is important. I think under today's conditions a starting of a new business in this country will cause for a fair amount of initial capital. I do not know whether you could really start a business for, say, \$300,000. \$300,000 in a high risk new business is quite a risk for any individual company to take, whereas operating through this consortium not only do you make more money, but each of the participants gets a spread of the risk among the various companies which the consortium finances.

COMMISSIONER MacKEEN: Your participation would become an asset?

MR. LEMMON: Yes.

MR. HOLMES: On the general principle of the large companies being required to put a certain percentage of assets into any particular type of security

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MR. LEMMON: Yes.

MR. HOLMES: On the general principle of the large companies being required to put a certain percentage of assets into any particular type of security

-- we would have a great deal of objection to any such provision.

COMMISSIONER GIBSON: On this question of financing new businesses and small businesses, would you care to make any comments about the operation of I.D.B.?

MR. McCARTHY: The activities of I.D.B. are a matter of public record, and my impression is that their activities have bean set up significantly in the past few years, judging from the amount of money they have been reported as advancing in the group. I would make the observation that it probably has been a useful thing, but whether it has been exploited to the whole possible extent in this country, I just do not know.

MR.BRYDEN: I do not think there is any significant difference between I.D.B. and the life insurance companies in the sense of competition. I think on balance they have been rather complimentary roles, with I.D.B. taking over those loans which appear to be a higher risk category and that would be barred to us for assorted reasons.

MR. GIBSON: You do not feel that the recent expansion of the last year has brought about competition?

MR. BRYDEN: That would not be my feeling; I do not know whether anyone else would have a different view. We have not been critical of their operation as far as competition with what we do is concerned.

COMMISSIONER BROWN: One company operating in Canada is probably specialized more than the others

provision.

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COMMISSIONER BROWN: One company operating

in this financing of small and medium type businesses and I wonder if Mr. Falkner would care to comment on the activities there?

MR. FALKNER: I do not know whether it is fair to say that one company has done it to a greater extent than others. As a matter of industrial policy, our company has selected a private placement group for our corporate investments and our investment departments are split in definite areas of operation and size of area. There is a department set up to specifically handle loans to small businesses.

In the States this has proven quite successful. We are doing it in Canada and it is a slow and hard job, but I would say on balance we are satisfied with the progress.

COMMISSIONER BROWN: What ranges.

MR. FALNER: They would range from loans in the area of $100,000 and possibly $\$\frac{1}{2}$ million. This is the area we are trying to cover. Of course, loans larger than those amounts are taken on as well.

COMMISSIONER BROWN: This is just debt capital?

MR. FALNER: Yes.

MR. BRYDEN: There is one additional point, Mr. Chairman, and that is, when we talk about our non-residential mortgage loans I don't know how many of them would be, in effect, loans to small business, but a large number of them would be the facilitating of the provision of buildings and so on for purposes of small business, but I don't know how you get at the actual amount that is included within those loans, and that does include things like warehouse loans, factory loans, loans on shopping centres and so on, all of which provide premises, if you will, for small business.

COMMISSIONER GIBSON: In the same vein do you make a fairly conscious effort to produce a good regional distribution of assets? You have a rather interesting table here showing distribution of your assets, which is fairly even on the whole. Is this a result of just the way the market forces work,

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or as a result of a conscious effort to push funds out across the country?

MR. BRYDEN: I think, Mr. Chairman, it is a little bit of both. I think all of us are conscious of being national concerns and wanting to get as wide a geographical distribution as possible, and the table to which you refer is ---

COMMISSIONER GIBSON: It is on page 68; 5.a.

MR. BRYDEN: Yes, and that we produced as an answer to some of the comments which have been made that on balance we seem to tend to pull savings away from some area of the country and invest them somewhere else, and we have had a bit of a problem in the initial instance in trying to develop that regional spread. Of course, mortgages can be easily spotted; your municipals and provincials; and then you have had to take your corporation list and attempt to break it up where the corporation operates in more than one province. You have probably had to use a population spread on your bonds, and so on, and that has produced this series under A of investment assets held by these companies in Canada. It comes out at the 7.8 million figure. Then we took our liabilities in Canada and went through rather a long process of apportioning them. The reserves were done differently as between ordinary insurance and group insurance and industrial insurance. The annuity reserves again fell under a different formula; our other liabilities to policy-holders, and so on, and we came up with this 6.9 billion

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liability to policyholders, and we have set out the ratio.

That, of course, will change from year to year as your business ages and as new business comes on the book and as investments are available.

We seem to be somewhat light in the Maritimes. On the other hand, it has been, it is our experience, extremely difficult over the last several years to get adequate availability of investments. All municipal bonds, and particularly Nova Scotia and New Brunswick, seem to be taken up locally. So, the availability of investment is a factor in this. However, I think it is quite significant -- the regional spread of the assets which have been achieved.

COMMISSIONER GIBSON: Do you charge pretty well standard -- I don't mean "charge": Do you take mortgages in pretty well the same rates across the country? In other words, there is not much regional difference in interest rates in the assets in which you deal?

MR. BRYDEN: I would think not.

COMMISSIONER GIBSON: For similar organizations.

MR. BRYDEN: I would think that is a fair comment.

COMMISSIONER GIBSON: So, to that extent the sort of national form of this industry is moving money around and not taking much account of one region being surplus or the other a deficiency in the determination of rates. You mentioned earlier in the United States there were sizeable regional differences. Do you

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do anything specifically more than this in trying to obtain a regional balance? You provide these monies at roughly the same rates for the same purposes right across the country. Do you do any more than that -- I am not saying you should.

MR. LEMMON: We get pressures -- perhaps that is not the right word. We are encouraged by our agency force to invest money where we do the life insurance business, and we advertise we do a mortgage business where we do a life insurance business. We do attempt to purchase municipal securities in the area where we sell life insurance for the purpose of supporting our local agency forces in that area. I can only speak for our own company, but that is certainly a factor in our investment operations -- the attitude of the local agent and the support for the local agent.

COMMISSIONER BROWN: We gather the place factor does enter into this distribution in the question of municipals. In other words, if you could buy municipals at 6 per cent in one place and in the Maritimes at $5\frac{1}{2}$, you don't buy them.

MR. LEMMON: We are not prepared, really, to sacrifice rate to aid this job.

COMMISSIONER BROWN: It is the price mechanism working.

MR. LEMMON: That is right. However, rate for the same quality of asset is pretty uniform across the country, so the question of municipals in the Maritimes is a bit especial.

COMMISSIONER LEMAN: Do you feel there should

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COMMISSIONER LEMAN: Do you feel there should

be such an effort? Is that theoretically sound?

MR. RIEDER: I think there is a natural force at work here. Capital attracts people to the section of the country where capital is being expended and, of course, the movement of people attracts life insurance sales; they just naturally go together. If a person is moving from the Maritimes to Ontario he brings his life insurance with him.

MR. LEMMON: It would certainly be simpler, particularly in periods of tight money, and cheaper to concentrate your investment operations in the most prolific and productive fields. However, there are other periods come about in this country whereby we are out beating the bushes for good investments, and in so doing we set up an organization, particularly in our mortgage organization, to lend money locally. In periods of tight money you don't cut off any of those local areas. It is not good business to cut them off. So, even from purely investment considerations, in periods when money is tight and investment opportunities are plentiful we make money available in all areas across Canada.

COMMISSIONER LEMAN: Yes, but I am thinking about the theory here. We talked yesterday about what the concept is of your client who buys an insurance policy. He is looking for protection.

MR. LEMMON: Yes.

COMMISSIONER LEMAN: And he wants to benefit from the fact you blanket the whole country in your investment policy, and therefore when people in one

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province buy insurance from your industry they would not like to see those investments made in their province as security for their particular protection, would they?

MR. LEMMON: No.

MR. BRYDEN: They look to the entire pool of assets for their security.

COMMISSIONER LEMAN: Therefore, how do you reconcile that with this insistance that there must be a fair distribution of investment practically porportional to the amount of insurance in force?

MR. LEMMON: There is another factor at work there in your theoretical borrower -- the theoretical purchaser of life insurance who may be looking to us to do the best possible for his funds will turn around the next day and be a borrower and complain bitterly if any life insurance company is not making funds available in his community. So, for the sale of life insurance, which is our fundamental business, it does make a lot of sense to diversify your interest.

COMMISSIONER LEMAN: I was wondering whether you subscribe to the theory or whether this table 5.a happens to be a very happy ---

MR. LEMMON: No, I think you have to bear in mind we are fundamentally life insurance companies, not investment trusts. The agency force continually reminds of that.

MR. BRYDEN: I think this is, though, a by-product of what has happened rather than a completely deliberate attempt, and a lot of it depends on the

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availability of investments, and, of course, say on the western coast in recent years there has been a high degree of availability of investment and at that point you find that total creeping up, but that will change from year to year -- not significantly, but as the increased flow comes along and investments are available in different areas.

COMMISSIONER BROWN: I wonder if we could turn briefly to another subject. I would like to start at paragraph 7.10. Reading between the lines there appear to be some criticisms here, and I would like to bring them out in the open if we can.

MR. BRYDEN: Mr. McCarthy, I think, is primarily responsible for the thinking about that area.

MR. McCARTHY: The question of availability of new issues is what is discussed in this paragraph basically. Some of the companies -- and I emphasize "some" of the companies -- have from time to time complained that when new large attractive offerings in the public market come along that they do not seem to be able to get what they consider to be a reasonable share of these issues at the time of offering. I have seen in my own experience examples of a $50 million issue of the Province of Ontario come to the market, and within 10 minutes be told that the supply has practically dried up. It is false logic to expect that in 10 minutes that has happened. What we would like to see is a modification, if not an elimination, of the arrangement that has been in force for many years whereby the investment dealers in their syndicate arrangement have

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arbitrarilly set aside for institutional distribution certain percentages of new issues, and part of these rules, as I understand them, go so far as to indicate to the members of that syndicate that they as individual members are not to approach the investment institutions and offer them securities; this is to be handled by an account manager. These rules, in the opinion of some of the member companies, have inhibited or retarded our ability from time to time to get an amount of an issue we want to get on the market.

COMMISSIONER BROWN: Well, this brings up several questions. I am on the other end of this telephone. Do I gather from this, first of all, the implied suggestion that the insurance companies should get preferred treatment on attractive new issues?

MR. McCARTHY: That is not implied at all.

COMMISSIONER BROWN: I did not think it was, but I just wanted to make it clear you were not implying that, because this was an implication that was read into the paragraph -- that you felt you should get better treatment than the general public.

MR. McCARTHY: No, that is not the implication. The implication is that we get a reasonable opportunity.

COMMISSIONER BROWN: Is there another implication you are not entirely happy with the use of the exempt list?

MR. McCARTHY: This is not, I don't believe, a uniformly held view with the member companies. In fact, some of the member companies do prefer it. Others regard it as a hindrance in the fulfilling of their demands

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COMMISSIONER BROWN: The next point is, is there an implied criticism of the wide syndicate arrangements for handling provincial issues as against tenders?

MR. McCARTHY: On the negotiated basis?

COMMISSIONER BROWN: Yes.

MR.McCARTHY: No, sir.

COMMISSIONER BROWN: You are quite happy with it?

MR. McCARTHY: I don't know the association has any sort of fixed uniform view on the matter. It has always struck me and our company as a pretty reasonable way of handling the problem of a continuing borrower such as a large province.

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COMMISSIONER BROWN: Have any others any comments on that?

MR. HOLMES: I am not in the actual trade but I have always had the feeling that when an issue came out and we wanted a large section of it and had to go out on the market to buy from speculators I have rather resented it, yes.

COMMISSIONER BROWN: This brings up the other question, the problem of riding the market. Is it the dealers who are riding?

MR. HOLMES: I do not know who is riding it. All I know is the ones who want the money to hold for some reasonable purpose -- not that we hold it particularly because we will sell it again --

COMMISSIONER BROWN: Because you will make a profit?

MR. HOLMES: No, not because of the profit but to buy something better. The point is when an attractive issue comes out the big investors seem to get cut down and other people get in there from whom you have to buy at a somewhat higher price.

COMMISSIONER BROWN: The complaint of the legitimate buyer is that on an attractive issue he can never get anything at all. In the same paragraph you mention prompt and full distribution. Is this tied up with the same thing?

MR. McCARTHY: Well, in the minds of some of the members it is. We believe short payment periods would perhaps eliminate what some of us feel

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is a tendency from time to time to speculation in the new issue market and that more proper and permanent distribution would be perhaps assured with a shorter payment period. There are occasions when this just would not be appropriate: in fact I can think of occasions when an institutional buyer himself might control the long payment period. It is an involved question.

COMMISSIONER BROWN: What would you regard as a suitable delivery payment period -- three weeks?

MR. McCARTHY: That would seem reasonable to me.

MR. BRYDEN: Is this not true in that also, that there is a certain time element that must elapse before the investment dealers themselves can obtain the certificates, etcetera, for the actual delivery. There is a purely mechanical problem.

COMMISSIONER BROWN: Yes, it is a purely mechanical problem that sometimes can be overcome.

MR. BRYDEN: But I think in the circumstances that it is within reason that the closer the delivery date to the offering date the better rather than letting it stand out for some time because I think the very length of time it stands out may tend to promote the sort of speculation, free riding et cetera that I am told goes on.

COMMISSIONER BROWN: Have you any particular comment to make on delivery payment?

MR. McCARTHY: I have no particular comment to make, no.

is a tendency from time to time to speculation in the new issue market and that more proper and permanent distribution would be perhaps assured with a shorter payment period. There are occasions when this just would not be appropriate: in fact I can think of occasions when an institutional buyer himself might control the long payment period. It is an involved question.

COMMISSIONER BROWN: What would you regard as a suitable delivery payment period -- three weeks?

MR. McCARTHY: That would seem reasonable to me.

MR. BRYDEN: Is this not true in that also, that there is a certain time element that must elapse before the investment dealers themselves can obtain [illegible], for the actual delivery. There is a purely mechanical problem.

COMMISSIONER BROWN: Yes. It is a purely mechanical problem that sometimes can be overcome.

MR. BRYDEN: But I think in the circumstances that it is within reason that the closer the delivery date to the offering date the better rather than letting it stand out for some time because I think the very length of time it stands out may tend to promote the sort of speculation, free riding et cetera that I am told goes on.

COMMISSIONER BROWN: Have you any particular comment to make on delivery payment?

MR. McCARTHY: I have no particular comment.

MR. BRYDEN: Well, it helps.

COMMISSIONER LEMAN: If there is not proper distribution what about the problem of wide distribution? Yesterday I got the impression that on an important issue of the right term that the insurance companies like that bond is pretty well stashed away until maturity or close to maturity until they become really short term bonds. If a syndicate felt that they wanted for the borrower really wide distribution how much could they let the insurance companies take of the first issue?

MR. BRYDEN: If that is one of the basic reasons behind the borrower's idea in the financing well, then obviously it seems to me you have to do something to hold down the institutional participation. We do not have to like it, but nevertheless it could be done.

COMMISSIONER LEMAN: Well, then would the market on it tend to make a market for you which you would not otherwise have? If your proportion of the issue was too large, the market would be pretty well restricted to yourself, would it not?

MR. BRYDEN: That is right, but it is this very thing, I think, in some cases that is tending towards what Mr. Falkner has described as private placement and that has been particularly true in the United States.

MR. FALKNER: Yes.

MR. BRYDEN: The amount of corporate issues held by institutions that have been acquired through

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MR. FALKNER: Yes.

MR. BRYDEN: The amount of corporate issues held by institutions that have been acquired through

direct placement as against through the normal type open market is very significant.

COMMISSIONER BROWN: There are a lot of legal problems through the S.E.C. registration.

MR. BRYDEN: Yes, the S.E.C., I think, tends to promote direct placement too.

MR. LEMMON: Which is a situation which does not exist in Canada.

COMMISSIONER BROWN: That is right, it has not gone to the same extent in Canada at all.

COMMISSIONER LEMAN: I was wondering why we talk about these important issues and less important issues. Is there an implication there that the syndicate manager in having an issue has created that sort of atmosphere you are talking about because he has not priced it properly?

MR. BRYDEN: A good issue can be offered at you/one price, at an interesting price, and when you get it in it may be at another price not too interesting. It is a matter of pricing in the market.

COMMISSIONER LEMAN: When they create this exempt list and decide how much the institutional participation is going to be and reserve that for the syndicate manager, what is in the mind of the syndicate manager then? Does he know that he has priced that issue too low?

MR. LEMMON: Not necessarily. It may be on a rising market which may create a less attractive price.

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COMMISSIONER LEMAN: Well, what would make your issue too low or too high?

MR. BRYDEN: I think you are going to have to ask the investment dealers what is in their minds when they do these things. All we can register at this point is that at times the existing arrangements do not make us too happy. Maybe we cannot be any happier than we are, I do not know.

COMMISSIONER LEMAN: I thought you meant at the same price. Are you saying that the syndicate having made a mistake in price we are sorry we did not get enough for it -- is that the size of it?

MR. BRYDEN: We should like to think so and if they underprice it we might be quite sorry they did not keep enough for us.

COMMISSIONER MACKINTOSH: Is not the syndicate manager likely to do what you just explained the life insurance companies like to do, to keep all your outlets busy and even if he could sell all the issue to one small group he does not want to?

MR. LEMMON: Quite right.

MR. BRYDEN: Yes, he has got a selling organization too.

MR. HOLMES: It just seems a little funny he has so many good customers when he has underpriced the issue.

COMMISSIONER LEMAN: Well, as a matter of fact, under the law an investment dealer is entitled to talk to some institutions about a prospective issue somewhat?

MR. BRYDEN: Oh, it is normal to in a number of cases.

COMMISSIONER LEMAN: That is right and that gives him a little chance to explore the receptivity of the institutions?

MR. BRYDEN: He is doing his homework on the price.

COMMISSIONER LEMAN: That is right.

MR. BRYDEN: But sometimes, as Mr. Lemmon says, between the time he establishes price there has been a time lag and the market may move. While you may have had it perfectly well placed in the beginning when the market moves and it does go it looks like a bargain.

COMMISSIONER BROWN: In the same paragraph you refer to earlier information. Is this a suggestion for a development of the counterpart of American inspection?

MR. McCARTHY: We merely make the observation that the operation of the capital market would probably be facilitated if lenders had a better outlook on new investments. We have not any blueprint as to how this might be done other than perhaps the dealer organization itself would work at the development of a calendar or a schedule of the more important borrowings ahead. This is not done in Canada to any extent at all.

COMMISSIONER BROWN: This has come up in several issues.

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MR. BRYDEN: I have the impression, Mr.

Chairman, that quite often prospectuses of a new issue really appear just about at the point at which you are asked to make up your minds whether you want to buy and I think it is our feeling that if that information were available a few days or a week ahead that the whole affair could be facilitated.

COMMISSIONER BROWN: Something along the lines of the United Kingdom system?

MR. BRYDEN: I do not know the United Kingdom system but I believe that is it. There are times, frankly, when you have already said you would buy a certain bond and you get the prospectus the next day. Of course, you are buying it from your own information and analysis at that point.

COMMISSIONER BROWN: Have you any comments to make about the handling of new Canada issues?

MR. BRYDEN: I do not think we have any particular comment at all on that. I do not know if anyone else has. Mr. Rapsey?

MR. RAPSEY: I do not think we have any comment on that, no.

COMMISSIONER BROWN: Have you any comments on security regulation generally? It has been suggested in various places that we might look at the possibility of developing an S.E.C. type of operation in Canada.

MR. BRYDEN: Well, Mr. McCarthy, I think you had some thoughts on that and possibly Mr. Falkner; he is familiar with the S.E.C. in the States.

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particular formula to set before you for consideration on these matters. I think we would prefer to see the participants in the capital market gradually evolve useful forms of doing business rather than laying down legislation. Laying the groundwork, rather than doing it through legislation.

MR. BRYDEN: I think our general view would be that an operation like the S.E.C. in Canada is really not needed and we think that a gradual evolution of our present securities laws would be preferable to the introduction of the blanket S.E.C. type security regulation.

THE CHAIRMAN: Well, at the present time there is not much in the way of regulation of the sort of issues that you would be interested in, is there?

MR. BRYDEN: Not too much, no.

THE CHAIRMAN: That is pretty well left to the investment dealers and unless they get into some trouble they are not interfered with as I understand it.

MR. LEMMON: That is pretty generally true.

COMMISSIONER BROWN: There is one point involved in releasing preliminary prospectuses on which there appeared to be some new thoughts. Would you like to see some changes in that direction?

MR. BRYDEN: I think we would like to have some preliminary prospectus before the time we are approached by an issue.

COMMISSIONER BROWN: On the question of trading

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there appears to be a tremendous variety within the industry and in your paragraph 5.19 to 5.21 -- particularly in paragraph 5.20 there is a rather peculiar sentence, the first sentence in the paragraph:

> "It is clear that this experience varies widely between companies, due to factors of policy, practice and personnel."

That "personnel" is fairly clear --

MR. BRYDEN: Mr. Rapsey, I think you were going to talk about our trading operation.

MR. RAPSEY: Yes. Well, it is true that the experience varies very widely between companies and I think this description that states about the policy, practice and personnel is quite true.

Dealing with them in order I think individual company policies have something to do with it. If a company is predominantly a mortgage investor and that has been their basic investment philosophy and policy then they are perhaps less likely to be active securities traders. I think investment practice has something to do with it. This hinges on policy to some degree too, but I think it perhaps varies as between the organization of the investment function within a company, how much freedom is given to the actual personnel in the investment department, how closely the investment committee of the board may wish to control the investment operations of their company and obviously there are going to be some delays if it is a question of getting approval before you do things or whether it

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is a question of reporting after you have done them.

By the same token, personnel makes a difference. You may have a person in your investment department who is a very successful and active trader -- he just thinks that way and in these cases those companies are going to trade more actively than others.

COMMISSIONER BROWN: Do I gather in paragraph 7.33 that the companies that do trade actively in Canada do so more actively than the American companies?

MR. RAPSEY: Which paragraph is this?

COMMISSIONER BROWN: I think 7.33.

MR. RAPSEY: Well, this deals with direct placement.

COMMISSIONER BROWN: The last sentence.

MR. RAPSEY: I think this again goes into the question of practice. If a company is one that has a very fully developed placement section in their organization, I think they are going to be giving less attention to trading than they otherwise might because their investment personnel is more occupied on developing the placement type of investment.

COMMISSIONER BROWN: Usually it is the other way around, that direct placement has not reached that proportion in Canada that it has in the United States and that therefore Canadians are inclined to trade more actively than Americans.

MR. RAPSEY: I think it is true that we do not have as much direct placement in Canada as they do in the United States. I see what you mean -- the reason being we do not have a direct placement -- I am inclined

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to say it is the other way around. I think it is a case of the egg and the chicken, it works both ways.

COMMISSIONER BROWN: Would there be some cases where the Manufacturers, for instance, do not get as much as others?

MR. FALKNER: We do not trade at all.

MR. BRYDEN: And yet I presume they are the largest factor in the direct placement system?

MR. FALKNER: Possibly.

MR. BRYDEN: I think you would say that a company which tends to run its mortgage portfolio up to, say, 60 per cent is generally lukewarm on the question of securities so that each company follows its own philosophy on this.

For our part we feel we are reasonably active in the trading field. There are constant changes going through where we are selling one security and buying another in its place. We may not be nearly as active as the Manufacturers.

Mr. Poyntz, how about Imperial?

MR. POYNTZ: We are quite active in trading and I think the reason we are is that we have developed the personnel who are building it up and it has been possible to have confidence in them and give them a range of activity within which they can operate without prior consent and they go ahead and do it. But if we had not those people we would not be able to do it, of course.

MR. RIEDER: We might be one of the extremes

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MR. RIEDER: We might be one of the extremes

on the other end of the totem pole. We are large mortgage investors, we are not in the United States bond market where trading is easier to do than it is in Canada and we probably have more close control over our actual investment operators than most companies.

COMMISSIONER BROWN: Would the size of the market and accounting problem be tied up in this?

MR. RAPSEY: I think size plays a part. Obviously if you are trading in, say, denominations of $10,000 or something like that it is not a very profitable operation for the time you spend on it and you like to trade in reasonable volume where we can differentiate between our markets obviously because in the United States where there is a very active, very diverse securities market we can trade very much more actively. In Great Britain where they have a wide selection of government securities in large volume you can trade very actively in British government securities but I think under the 2 per cent stamp duty over there, which does not apply on government but applies on corporation securities, this inhibits the trading in that field. In Canada it varies a bit. We can trade in Canada on the provinces, Ontario Hydros and even to a degree incorporate bonds where sinking funds are operating and that sort of thing.

THE CHAIRMAN: We will now adjourn for fifteen minutes.

(At this point a short recess was taken.)

--- After Recess

THE CHAIRMAN: The meeting will resume.

COMMISSIONER MACKINTOSH: Mr. Chairman, I have a few questions I should like to ask in respect to Section 6 of the submission at page 89.

I notice the setting out of the objectives of economic policy and the comments made elsewhere in the brief which suggest that the industry attaches particular importance to the maintenance of reasonable price stability. How far do you think this is likely to be usually compatible with the other objectives that you set up?

MR. BRYDEN: Well, Dr. Mackintosh, it always seems to me that any country should have a series of objectives just as any business should. Now, it may be that at various times in the actual practice of management of the economy you will find that you seem to be incompatible in some respect or another but, alternatively, I do not think that undermines the objectives. I think you must still have the objectives and you should try in your fiscal and other management to pursue your way toward both objectives. I think that the maintenace of a high level of employment and income is one of the major objectives that we should have, and also the maintenance of reasonable price stability. It seems to me that those are the two, and the rest sort of flow from those. I do not think we should attempt to have one without the other because each time we do it produces a whole series of imbalances in the general harmonious objectives and the growth

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of the economy.

Price stability is important of course, as far as the life insurance companies are concerned, bearing in mind that we speak on behalf of the fixed dollar savers and it is true I think that every period of inflation can be most harmful in wiping out past capital values as unemployment can in the initial instance. I think you have to try to steer a course that recognizes both of these objectives, although your steering of the course is not going to be completely perfect all the time. I think that once you see an imbalance coming you have to try and do something about it to get yourself veered back on your course.

COMMISSIONER MACKINTOSH: More recently there wa the tendency to elevate your third objective, namely the promotion of a sustained and sustainable rate of growth, pretty much to a level with the first two. A few years ago that probably would not have been the case.

MR. BRYDEN: I would have thought that the third one, the promotion of a sustained and sustainable rate of growth within the economy, really flows from the first two.

COMMISSIONER MACKINTOSH: Yes. You could argue that it is difficult to attain any of the three without some measure of success with the others.

In the matter of responsibility for monetary policy, you say that the Bank of Canada should be independent in the sense that it can pursue objectives, but that in the case of any division of opinion the

of the economy.

The stability is important of course, as far as the [illegible] mind that we speak on behalf of the fixed dollar savers and it is true I think that every period of inflation can be most harmful in wiping out past capital values as unemployment can in the initial instance. I think you have to try to steer a course that recognizes both of these objectives, although your steering of the course is not going to be completely perfect all the time. I think that once you see an imbalance coming you have to try and do something about it to get yourself veered back on your course.

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In the matter of responsibility for monetary policy, you say that the Bank of Canada should be [illegible]

government views must be paramount. Do you find anything in the statement which the Governor made following his appointment and the subsequent statement by the Minister of Finance which would differ from your views as to the probable relationship here? You are apparently familiar with that topic?

MR. BRYDEN: I thought, Dr. Mackintosh, that when we wrote this piece about the responsibility for monetary policy it was on all fours with Mr. Rasminsky's statement and the subsequent endorsement by the Minister of Finance.

COMMISSIONER MACKINTOSH: Well, that is what I expected to be confirmed. I am interested in what you have to say about a directive from the Government, or the Minister of Finance to the Governor. Do you look at this as a fairly formal act? A great many people say "directives". I am not very sure whether they mean a nod or a notarized document.

MR. BRYDEN: I would think that if the situation reaches the point where there is sufficient difference of opinion between the Government and the Governor to lead to a directive being issued, that should be at least in written form, not necessarily notarized. That is the point really, it seems to me, where if the Governor then cannot accept the implications of the directive because of the responsibilities he is carrying by the preamble of the Bank Act, then it seems to me that he must tender his resignation and, in so doing, I think he tenders it for reasons. As soon as he does then the whole matter comes up for

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public debate.

COMMISSIONER MACKINTOSH: Now, that is the point I should like to clarify. Do you think of this directive as being a public directive or not public until the Governor has made up his mind to resign?

MR. BRYDEN: I had not thought about that particular point. I would think that it should be a directive from the Government to the Governor private in the first instance and then to the Governor himself to either follow the directive or to resign, at which point the thing becomes public. I think probably it is better kept private up to that time.

COMMISSIONER MACKINTOSH: Would you not think that the probable result of providing for this legislation would be that the power would never be used unless it was desired to prepare the way for the forced resignation of the Governor?

MR. BRYDEN: I would not think that this particular point would need to be spelled out in the legislation. It would seem that it is the basic operating procedure; an unwritten rule, if you wish. I think it would be very difficult to frame this in a statute to give effect to this kind of situation.

COMMISSIONER MACKINTOSH: You mean you would not provide any statute for the issuing and authority of a directive? I quite agree it would not spell out the mechanics.

MR. BRYDEN: Well, yes, I think that could be put in the statute in a pretty innocuous form, making the provision that the Minister may from time to time

issue a directive having regard to this, or something of that kind. I think it could be handled without spelling it out in too much detail, but it is much better I think kept as a sort of unwritten rule.

COMMISSIONER LEMAN: Have you any idea what the form of such a directive might be? Obviously we are tàlking about a case here where in the opinion of the Government the Governor of the Bank has followed in his field of policy a course which does not quite fit the general policy of the Government. Do you imagine a specific type of conflict there, and therefore imagine also what the directive would be? What would it say to the Governor? Could it be so vague as to say, make money easier or make money tighter? What would it say?

MR. BRYDEN: I would think that under those circumstances if such a directive were to be issued the Minister of Finance would want to give reasons for his conclusions as to what monetary policy ought to be under the existing circumstances, because if the Governor does not agree to accept that then he is going to come forward with views as to what monetary policy ought to be in his view under the same set of circumstances. I would think that it would not be a vague directive. I would think the Minister of Finance should make a case within it for the direction that he would wish monetary policy to take.

COMMISSIONER LEMAN: Would it be still fairly precise, do you think?

MR. BRYDEN: I think if I were writing it

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I would make it pretty precise.

COMMISSIONER LEMAN: In quantitative terms?

MR. BRYDEN: You mean, 2 per cent more money supplied or something like that?

COMMISSIONER LEMAN: Yes.

MR. BRYDEN: No, I do not think you would do it on that basis. I would think you would give the reasons why you think there ought to be, say, more money ease than apparently the Governor is prepared to let exist, and then he will come up with his points as to why he believes the current policy fits the current scene. Therefore in public discussion you then have both sides of the question.

COMMISSIONER LEMAN: The secretary just mentioned to me something I had not thought about. In Australia apparently such directives have to be tabled in parliament.

MR. BRYDEN: Just as soon as they are issued?

COMMISSIONER LEMAN: Yes.

THE SECRETARY: Within 15 days of the house sitting.

MR. BRYDEN: Well, I would assume that even under what I have suggested it is going to be tabled within about 15 days, because if through mutual discussion you have arrived at an impasse I do think the Governor's emerging views and his intent ought to be constantly before the Minister, and if it gets to the point where a directive is issued I am quite satisfied that the Governor is almost going to implement

his side of the case immediately. Whether you want to force a tabling of it or not, I do not know.

COMMISSIONER GIBSON: You said earlier that you thought it would be desirable not to make it public until the Governor had a chance to consider whether or not he wanted to accept it.

MR. BRYDEN: That is right.

COMMISSIONER GIBSON: Of course, if he accepted it it would be highly undesirable to make it public at this point because then he would appear to be forced to do something which would lower his prestige.

MR. BRYDEN: Yes. I think the point at which it should be made public is at the point where the Governor cannot accept it. If he can then I do not see why such a directive ought to be public property at all, because presumably at that point the monetary policy of the government and the Bank are in unison.

COMMISSIONER LEMAN: Is it desirable for the Government to really give precise directives to the Governor which presumably are necessary because they cannot quite agree, and yet there is a private directive put on the Governor's desk and he accepts it and nobody knows that this has happened?

MR. BRYDEN: Well, you know when you get into this area of central banking and monetary policy I think so often there is so much said and so much misinterpretation, my view would be that it is better a directive of that kind, if it were ever issued, to be a private document until such time as the Governor decided that he could not accept it. I think if you

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publish it prior to that you have really put the whole discussion out in public in any event and it may not be appropriate at that point for such divergences of view to come out in public.

COMMISSIONER MACKINTOSH: That probably means that the Government or Minister of Finance should not issue a directive until it has been determined that the Governor cannot accept it.

MR. BRYDEN: I think in all probability that is the way it would work in practice because they have reached an impasse, or else a directive is not forthcoming in any event. It is sort of the last step on the part of the Government and presumably the last step on the part of the Governor.

COMMISSIONER MACKINTOSH: We have had a number of suggestions from various sources as to improvements to the board of the Bank of Canada, vaguely stated and many of them, or at least not very precisely stated, including suggestions from more people with finance and/or banking experience, including the daring suggestion of putting a Communist on the board. I take it the present board is predominantly regional?

MR. BRYDEN: I believe that is the case.

COMMISSIONER MACKINTOSH: I take it, of course, the Act requires that, or does it?

MR. BRYDEN: I am subject to correction, but I believe it requires people of diverse occupations; I am not sure that the Act itself requires regional representation. I think it started that way. I am subject to correction on that, but I believe that is the case.

COMMISSIONER MACKINTOSH: Has the industry any ideas as to a different pattern of directorships, and would this lead to a large number of people of financial competence and experience?

MR. BRYDEN: I don't believe, Dr. Mackintosh, that the industry as an industry has any views on that particular subject; it wasn't discussed in our meetings. I think, though, that from what we have said in the brief that the industry would probably agree that competence in finance and economics would be desired to a greater extent than geographical or even occupational representation, and that in that event the chartered bankers are excluded under the Act and investment dealers, although not excluded, I think would be very likely to exclude themselves on the basis of their own particular interest with the Bank of Canada and this certainly narrows the area of competence -- that is to be found in the matters of finance in any country, and I would think that that would lead to the suggestion that the board might be smaller than it is and based essentially on competence in economics and in financial matters. That is not an association view, I think that is probably a personal view drawn from the general position that we have taken.

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COMMISSIONER LEMAN: Well, would you visualize, say, a full-time one?

MR. BRYDEN: That had not been in my mind, no. I would think that you might have a board of six or nine, or as many as you wish, but not a full-time board, no.

COMMISSIONER LEMAN: Where do we find those people where there is any conflict of interest which would arise?

MR. BRYDEN: You might find them in the life insurance companies! You might find them amongst economists and university professors, but it does create quite a problem once you have really excluded your chartered bankers, and also I think that the investment dealers would exclude themselves, so that the area becomes much smaller in which you can make ultimate choices. Again that is the prerogative of the Minister of Finance, whoever he may be.

COMMISSIONER LEMAN: If we could find them in the life insurance industry, would that cast a reflection on the responsiveness of life insurance companies to short-term monetary movement?

MR. BRYDEN: I would doubt it.

COMMISSIONER MACKINTOSH: Turning to another topic, we have had representations that the bank should cease to act as the government agent on debt management and that the Department of Finance would run the operations itself. There were others that felt that we might have a board of debt commissioners, or something, charged with this so that the Bank might carry out its

operations, but on a much more detailed direction from the Department. Have you any view on that?

MR. BRYDEN: That, too, is a subject, Dr. Mackintosh, that the association did not discuss. At the present time the Bank of Canada operates on an agency basis. I think you can develop a pretty clear case for having debt management operations come under, say, the Department of Finance, and alternatively you have the overriding proposition that a unification of monetary policy, fiscal policy, debt management policy, and so on, is essentially now in the throes of being under finance and you then have to develop a means of achieving that through necessary co-ordination, and I think that is the point that I don't think I am competent to have an opinion on.

COMMISSIONER MACKINTOSH: It is a little hard to see how, if you have two groups operating, you are not simply requiring they confer by telephone first before either of them takes any action.

MR. BRYDEN: On the other hand, with it centred, you have in the present instance one man wearing what, three hats; he wears the monetary policy hat, he wears the debt management hat as a agent and he also wears an exchange rate hat, again as an agent. Co-ordination is essential. How you achieve that co-ordination to the best effect I think would be the basic position as far as its eventual location is concerned.

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COMMISSIONER MACKINTOSH: That is the problem, I think, almost in any business; the head of the business

has a variety of headgear he has to put on.

COMMISSIONER GIBSON: Do any of your other members have personal views they would like to express?

MR. BRYDEN: I would be very happy if they would. Apparently not, which suggests that possibly they are agreeing with me.

COMMISSIONER BROWN: They regard you as the expert.

MR. BRYDEN: That is right.

COMMISSIONER MACKINTOSH: You mentioned the need for co-ordination and unifying policies. Would you feel that recent monetary history reflected basic conflicts between objectives or that the mix had been wrong?

MR. BRYDEN: I would think that probably what you would say is that the mix might have been somewhat different. Now, that is hindsight and it is so much better than foresight.

Again, it seems to me that your major aim is to keep your entire economy in a state of balance and if things seem to be getting out of line in any one area, some offsetting action, if possible, should be taken and it is kind of a constant walking on a tightrope -- if you will -- as between all these various facets of the economy and as in any business, if you let one thing get out of line, normally you take a wack at that and hit it on the head if you can to bring yourself back into that unified balance that seems so essential, and I think that recent history indicates that we are somewhat out of balance.

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There is also a question of timing involved here; there are times when you should do something and there are other times when you shouldn't, and that is part of this walking on the tightrope.

COMMISSIONER MACKINTOSH: I am not sure that is a very helpful prescription; I accept the truth of it, though.

COMMISSIONER LEMAN: It seems to me in the brief that you feel that in order to have the proper mix of policy you have to have a degree of responsiveness to the policies that are being pursued, and in paragraph 6.19 there is a direct reference to that; you talk about responsive elements of the economy and responsive financial intermediaries, and we have talked -- I don't want to go back into all the details, but we have talked about a good deal of the areas in which your particular industry might be deemed responsible or not. How would you judge that from the point of view of the two big areas of where you should have responsiveness; say that on the liability side there doesn't seem to be much responsiveness to short-term movements.

MR. BRYDEN: I would think on the liability side that there is not a high degree of responsiveness; I think the liabilities, of course, are created by the sale of insurance and, as you said yesterday, we sort of keep constant pressure on these sales, and the economic conditions that the country help or hinder a bit and with continuing pressure for sales, but on balance the liabilities accrue from that type of operation

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and on the basis you suggest it could be considered to be relatively unresponsive in the sense that you are using it.

COMMISSIONER LEMAN: And that was even true of loans to policyholders, which are a matter of contracts, too.

MR. BRYDEN: I don't quite get the connection on the loans to policyholders; that is also a contractual arrangement.

COMMISSIONER LEMAN: That is right.

MR. BRYDEN: It does seem from our operating experience that most policyholders are inclined to use their policy loan privileges as a sort of a loan of last resort, if you will.

COMMISSIONER LEMAN: And therefore would you say we cannot look for much responsiveness there in that particular area either, except to the extent that you might get more demand for loans at a time of tight money?

MR. BRYDEN: I mean that is what you do under extreme conditions, and back in the 30's there was a time when at least 20 per cent of the assets of the companies were in policy loans.

COMMISSIONER LEMAN: But not rate-wise; you can't respond rate-wise in that area?

MR. BRYDEN: No.

COMMISSIONER LEMAN: So, we have to look on the asset side basically, investments, and this morning we talked about trade; the record of trade among the companies represented here was very uneven,

some were not very active traders and others were.

COMMISSIONER LEMAN: Could you summarize a bit in what way you feel the industry might be responsive on the asset side?

MR. BRYDEN: Well, it has been my impression that the industry as a whole was reasonably responsive to monetary policy; certainly as interest rates go up and/or go down it does start a chain of operation running back through our investment policy. Part of that, of course, will have to do with the new money which we invest and the other part comes from the total gross investments, if you will, which includes the amount of trading that is done. It finds itself in that area and it also finds itself expressed, I think, in the degree to which companies tend to have forward commitments, particularly in the mortgage market, but that also is true to some extent in securities and at some periods we may have our cash income, if you will, the net cash income committed ahead for six to nine months; at other points you would let these forward commitments run out.

On the whole, though, I would have thought and do think that the life insurance industry is reasonably responsive in the capital market to shifts in interest rates and in some degree to shifts in the economy.

COMMISSIONER LEMAN: We discussed your mortgage operation this morning, and it seems as though the rates and mortgages do not respond quickly, is that right?

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COMMISSIONER LEMAN: We discussed your mortgage operation this morning, and it seems as though the rates and mortgages do not respond quickly, is that right?

MR. BRYDEN: They respond to -- they certainly respond to the general trend in interest rates, although there is a time lag and again part of that depends on the demand for mortgage money within that particular market, but we would find, I think, over long cycles of interest rates that you have mortgage rates that have run all the way from 7 per cent, such as might exist now, and I can remember the point at which mortgage rates were 4½ per cent on good loans during a period of low interest rates.

Now, there is a lag. Part of that lag, I suspect, is due to the fact that it takes time to bring a mortgage investment into your actual operating position. I mean, first of all, there is the examination of the loan, then there is your commitment and then there may be six months lapse before your cash starts to go out as this is in the process of construction, and there is quite a time when the interest rates, of course, would be fixed at the point of the original approval, so that contributes in part to that lag, but the mortgage rate in Canada is not what you would call a particularly responsive rate.

On the other hand, if we can over the years develop a secondary mortgage market and a larger number of people participating in it, then that in itself will produce more responsiveness in what at the moment might be regarded as a rather sticky interest rate.

COMMISSIONER LEMAN: A system of discounting mortgages?

MR. BRYDEN: Yes.

COMMISSIONER LEMAN: Well, the NHA mortgage rates, they have been rather sticky and they do have an influence on the conventional mortgage market to a large extent?

MR. BRYDEN: That is right.

COMMISSIONER LEMAN: And therefore we don't very high responsiveness in that area either.

MR. BRYDEN: Mind you, one of the things that you have to have in a responsive mortgage market is some sort of uniformity in the piece of paper. A conventional mortgage is a mortgage on a particular piece of property in a particular place and to a particular person. Now, the liquidity of such an instrument is pretty small, because anybody who would wish to take it over would really have to go and look at the property and assess the credit worthiness of it, and so on, and once you move into this N.H.A. insured mortgage position you are creating a fairly high degree of uniformity by that insured position. This is essential. That sort of a thing would be essential before you could really move into a place where your mortgage documents are to some extent liquid.

Now, if you could move further to the point where no matter what the interest rate may be, if they are in the sort of a package that can be bought either below par or above par, then you can get gradations in that interest rate between that which is normally imposed of, say, one-quarter or on-half per cent, and then you develop in that way to a more flexible, more responsive interest rate in that field.

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Do you wish to say anything about that, Mr. Lemmon?

MR. LEMMON: Just one small extension on that. It is inevitable, perhaps, in all of these discussions that we compare ourselves with the larger country south of the border which has gone through some of these problems before.

The F.H.A. document in the United States is a much more marketable document and is much better than the N.H.A. document in Canada. Why should that be? One main reason is that the National Housing Act prevents loans being made below the face amount of the loan; it can't be made at a discount.

In the United States the F.H.A. loans are made at discounts and the discount charges are as quoted; you can get an average price at which F.H.A. loans change hands from the various concerns in the United States and that, in my opinion, tends to make interest rates on mortgages in the United States more quickly responsive to movements in the bond market because you have a uniform document that is generally acceptable and it is available at a price which could be a discount or could be a premium.

MR. RIEDER: On this whole question of responsiveness, Mr. Chairman, we are fairly responsive to shifts in interest rates within different categories of investments, but, by and large, an insurance company remains fully invested all the time, and the money that emerges is invested. Our cash balances don't vary a great deal. So, in that sense you might say we are not too responsive.

COMMISSIONER LEMAN: I want to get at this a little further on in this discussion, but there is the matter of controls otherwise than through these basic financial policies. The fact that N.H.A. mortgages have been used to a large extent to encourage new construction and the fact they have been sticky, could we consider they did not tend to make that particular industry responsive -- as responsive as it could have been to monetary policy?

MR. LEMMON: I think that is a fair conclusion.

COMMISSIONER LEMAN: There seems to have been a government policy of longer range to try to help the residential construction industry in Canada a little bit regardless of what was going on from year to year in the needs of monetary policy.

MR. BRYDEN: I would say so. It seems to me that the degree of housing activity within the country at any time is a very important part of the total of capital invested, and I think the use of the N.H.A. has been part of what has been done in order to stimulate the building of houses for purposes of your capital investment booms -- well, the capital invest-

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COMMISSIONER LEMAN: There have been changes of rates on N.H.A. mortgages.

MR. BRYDEN: Yes.

COMMISSIONER LEMAN: The record of changes -- does it seem to have been co-ordinated with monetary policy?

MR. LEMMON: With considerable lag -- varying lags; but, considerable lag.

MR. POYNTZ: An evidence of responsiveness in the face of a fixed rate is the participation of the lender. They respond by not participating or participating to a greater degree.

MR. BRYDEN: And that really reflects where the conventional loan rate may be in terms of the N.H.A. rate. There would be times when conventional loans would be more attractive. There would be other times when the N.H.A. loans would be relatively more attractive.

COMMISSIONER LEMAN: Again in this field of responsiveness I get the impression from your arguments here that you feel that to the extent your industry is responsive it is mostly to long-term interest rates. Generally speaking, monetary policy begins to act at the short end, doesn't it? How do your visualize this mechanism? How do you think you can -- with how much lag would you be responsive if you are responsive to the long type of rates rather than the short?

MR. BRYDEN: Well, I suppose we would be as responsive as the degree of lag between short-term

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COMMISSIONER LEMAN: Again in this field of responsiveness I get the impression from your arguments here that you feel that to the extent your industry is responsive it is mostly to long-term interest rates. Generally speaking, monetary policy begins to act at the short end, doesn't it? How do your visualize this mechanism? How do you think you can -- with how much lag would you be responsive if you are responsive to the long type of rates rather than the short?

MR. BRYDEN: Well, I suppose we would be as responsive as the degree of lag between short-term

rates and long-term rates: That just sort of normally happens. We would in the first instance vary our committed position. In the second instance we can acquire larger amounts of either cash or short-term securities. Other than that we proceed to operate within the long-term end of the business and then different rates for different categories of assets tend to vary with each other, and you sort of, I suspect, would consider you would go up the scale as the rates widen. I think they would first appear in, say, your federal government debt. You would have your provincial bonds starting to reflect that pretty normally. You then have a downward movement of your municipals and corporations. There is a lag in all of those, but I think it is part of our operation within that market, even trading from one to another, that tends to pull the other type of interest rates in line with the basic long-term rate that exists from time to time as a result of monetary policy.

COMMISSIONER LEMAN: Yes, but with your experience as to what this lag is, we have heard from others a great deal about the value of signals -- the monetary policy operating as a signal. They operate first at the very short-term end. Do you observe these signals as something you can predict will influence your operations nine months or twelve months later?

MR. LEMMON: It did not take any nine or twelve months this spring. It took about nine or twelve days.

COMMISSIONER LEMAN: But you just talked

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COMMISSIONER LEMAN: And yet that [illegible]

about lags: How fast does this pervade into the long-term interest rate field in which you are responsive?

MR. LEMMON: I don't think you can set a specific time. I quoted this spring as an example of where the range on the long-term market came after a change on the short-term. It has not always been that fast. Sometimes it was six months, and sometimes you have had a swing in the short-term market that has not ever had a corresponding effect on the long-term market.

COMMISSIONER LEMAN: So it would be your own judgment in the circumstances you are facing at a given moment that these signals coming at the very short end will produce this effect quickly, more slowly or not at all in the long-term field. You would make that judgment yourself?

MR. LEMMON: Collectively the market would make that judgment.

COMMISSIONER LEMAN: How about your industry in particular? Do you think you would have a particular judgment based on the type of the sectors of the economy with which you deal -- the insurance field and the kind of investments you make?

MR. BRYDEN: I would think most of the investment officers of the life companies are fairly knowledgeable in the field of interest rates, and I think all of us are attempting to work with the same or virtually the same basic figures that your central bank does, and we are just as conscious -- not quite as

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conscious of a change or the prospects of a change in the interest rate level. I don't think, for what it is worth, that where the central bank gives a signal as such really has an awful lot of weight. The signal only comes after a certain situation has developed. We, I think, are watching the basic situation and to some extent may even anticipate such a signal in determining what we think the trend of interest rates is likely to be, and having made a determination on that we then move to the extent we can to capitalize on the expected trend.

COMMISSIONER MACKINTOSH: That is to say, if there was a significant rise in the short-term rate of interest you would lighten on long-term bonds and invest short-term in the expectation you could later go back into the long end of the market at a better price?

MR. BRYDEN: Yes. You tend to trade between shorts and longs. You tend to trade between credits. You tend to trade between different categories based on the spread of interest yield which could be is either wide or narrow.

COMMISSIONER GIBSON: But you just don't respond to a signal. You make your judgment in the light of the various factors in the market-place, in the light of what the central bank is doing and saying, but the signal is only one relatively small part of this whole thing?

MR. BRYDEN: I think the signal in most cases would really confirm or otherwise the judgment

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which you had already made.

COMMISSIONER GIBSON: Or which you were in the process of making?

MR. BRYDEN: Yes.

MR. LEMMON: Perhaps a situation that developed in England over the last few years could illustrate this, because I think it is true they have used monetary policy more drastically than countries on this continent in recent years.

The first time the Bank of England rate went to 7 per cent the rate on long-term British Governments didn't go very much over 5 per cent because the attitude of the market seemed to be that the situation they were contending with by means of the short-term rate was a relatively short lived situation and would likely be corrected within nine months or a year and that the long-term rate would not likely follow it. The next time the Bank of England rate went to 7 per cent the long-term market was not nearly as optimistic and felt the difficulties were much more deep-seated and not apt to be corrected so quickly, and the rate on British Government long-term bonds was up around 6-3/4 per cent.

COMMISSIONER LEMAN: You make a reference here to perverse regulations: Is this the general area you had in mind there?

MR. LEMMON: That is right.

COMMISSIONER LEMAN: You also state that different national intermediaries are, of course, through responsiveness to the short-term or long-term

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structure not affected quite so immediately or so directly by monetary policy changes, the chartered banks being the very first. In this chain, among institutions as against individuals, would you be about at the end of the line?

MR. BRYDEN: I don't know you can have any particular judgment on that. Certainly, as you say, the Central Bank's actions affect first of all the chartered banks. I suppose -- and I am only supposing -- the next place it may be felt is in what has been termed normally "near banks" who conduct relatively the same type of business. Then I think you move out to other financial institutions. Whether the individual -- where he would fit, I don't know. So, whether we are at the end of the line or not, I don't know. I do think, though, that with the type of investment management that seems to exist throughout the industry I would doubt very much if we are at the end of the line.

COMMISSIONER MACKINTOSH: But surely the communication of a change in interest rate is instantaneous? It does not run down a queue?

MR. BRYDEN: No.

COMMISSIONER MACKINTOSH: Everybody gets the same signal?

MR. BRYDEN: But some people are in a position to react to that, I would suspect, a little faster. As far as life insurance companies are concerned, I think it has to be borne in mind that we are almost constantly fully invested. That is what we have to do. We cannot afford to stay with idle

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cash for long because it has an effect on our interest earnings, and the interest earnings are a very high part of our competitive position with other companies. So that you do have always a large body of investments which you are holding. You do have a cash inflow coming in pretty regularly. You can deal with your cash inflow quite easily and quite quickly. To get at your existing investments you then must determine whether there are trading opportunities, and, to the extent there are, those companies who trade proceed to do exactly that, and in that way bring the whole structure of interest rates back into some reasonable balance -- the kind of a balance that existed probably before the change in trend occurred.

COMMISSIONER MACKINTOSH: So, one answer is that within the industry those companies who have a very active trading policy do respond very quickly?

MR. BRYDEN: Very quickly.

COMMISSIONER MACKINTOSH: If a company does not trade, of course, it does not respond.

MR. BRYDEN: And I think on that basis, even though the degree of trading is different with different companies, that one table that showed our gross investment in terms of our net investment in a year showed something like three to one, and it was about 2-$\frac{1}{4}$ to one excluding the federal bonds and treasury bills. So that, that is some measure of the trading impact that goes on.

COMMISSIONER MACKINTOSH: Another thing which I think would be of some use to point out: You

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COMMISSIONER MACKINTOSH: Another thing

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say you are always fully invested, but you stand pretty high among the groups in having a highly dependable cash inflow?

MR. BRYDEN: That is right.

COMMISSIONER MACKINTOSH: And this affects your investment position. There are a lot of institutions that may not be invested, but they haven't got this additional cash inflow.

MR. BRYDEN: We have a very predictable cash inflow and that is what makes it possible, (a) to be quite fully invested and (b) to even anticipate, as forward commitments, that cash inflow over a period.

COMMISSIONER LEMAN: To supplement the mechanical workings of monetary policy, you make reference to both the open-mouth policy of the monetary authorities and the moral suasion system -- an expression I don't like becuase it is not English. But, as I gather, you make the point that moral suasion should be done in private, if at all; is that right?

MR. BRYDEN: I would agree, yes, but again I don't know -- yes, this is an industry view in the sense that it was put into the brief.

COMMISSIONER MACKINTOSH: I am not quite sure what that means.

MR. BRYDEN: Everybody else nodded, so I guess that is all right. I think this whole matter of publicity as far as the operation of the Central Bank is concerned is rather difficult. Throughout the brief we have said that the Bank should make the fullest disclosure of what it has done and as fast it

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can. Also, that the Governor should keep the Bank's emerging views on monetary policy constantly before the Minister. I think we have said that public statements of intent should only come at rare intervals at the point at which there is some major change in policy or major event occurs. I think we have said if changes in the discount rate can be made meaningful then that would be so much the better as an indicator, and that discussions with interested groups should be conducted, and I think are most effective when done without undue publicity. It has always been my feeling that central banking is a very complex business even for the experts, and the more that is said the more misinterpretation is likely to be drawn from those statements.

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And monetary policy is sufficiently complex that it just about cannot be expressed in headlines. No individual other than the Governor, it seems to me, is in a position of appreciating in the round all the various factors that are bearing on the continuous decisions which he has to make and make in the light of his assessment of what the current situation is.

Discussions with interested groups such as the banks -- and I understand that he has them fairly regularly with his money-market dealers, if you will -- are one thing. Those people are in a special situation in the sense that they have a continuing relationship with the central bank and also a background of the sort of mutual understanding and knowledge, but I think that any publicity concerning that kind of discussion would, in the first place, inhibit the discussions and, secondly, would lead very easily to a wide-scale misinterpretation of what the real intent of the discussion was, and as I say, I think those are the reasons why we feel that the Bank of Canada should be able to conduct its affairs in reasonable anonymity.

Remember, too, there has to be two sides to a market; there has to be a buyer as well as a seller and there is a difference of opinion which creates the market and it would seem unconscionable to me if the central bank had to trot out its intent and everything else in the open because I think that would cause a much faster reaction in the market and one that could quite often be misinterpreted -- in fact it could almost

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ruin the market, you would not have a market.

COMMISSIONER LEMAN: You say in certain circumstances moral suasion could be resorted to. How effective do you think it is?

MR.BRYDEN: I think it is quite effective amongst those groups who have that sort of continuing relationship. Moral suasion -- again I agree with you that that is a very difficult word to use, but, for example, and going back to the life companies' own experience during the war, there were several meetings held with the Minister of Finance with regard to investment in war loans, and as a result of the understanding that we got of the subject at that time et cetera virtually all of our available cash during that period was funnelled into war loans. It was done quite willingly on our part. It was done a little ahead of receipt of our income and on the whole that worked extremely satisfactorily.

There are other conditions which might exist which would have the same effect, but I believe I do not think that moral suasion should operate to try to get any group to do anything which is not in their own best interests to do, and I imagine that any Governor of the central bank would tread very carefully on that score so to that extent "suasion" is really not a good word.

COMMISSIONER LEMAN: I think I would like to make an exception for war time. Things may be changed during war time. Let us talk about peace time. You bring in one example here about the conversion loan

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where you say that the insurance companies as an industry were brought to Ottawa about the conversion loan. Is that a fact?

MR. BRYDEN: Yes, that is right

COMMISSIONER LEMAN: That is in the brief, is it not?

MR. BRYDEN: Yes.

COMMISSIONER LEMAN: This was not much before the conversion loan was out, was it?

MR. BRYDEN: No, that was at a time when it was contemplated it was about to be done, and the representatives, or at least some of the representatives of the insurance companies, together with other financial institutions were brought to Ottawa, and the whole operation was explained in very considerable detail and I think that that was a very effective method at that point of building and giving a complete background on that conversion operation. It was much better to have had that background of the operation than to all of a sudden have it hit you in the face that such and such a bond issue was being converted. As to what results it had, it is a little difficult to say. I think as a result of that the chances are there were more bonds bought by the companies than might have been bought had it merely come as another issue.

Would you agree on that?

MR. LEMMON: The records show that we did not buy it in those two periods.

MR. BRYDEN: Well, that is the on-balance figure, but I have forgotten what the subscriptions were

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but I think a large number of the companies participated in the purchases of conversion bonds. Now, to the extent that we at the same time let something else run off is another matter.

MR. HOLMES: In other words, it was a conversion operation. We had the old bonds in that case.

MR. BRYDEN: In most cases on the bonds there were cash purchases too.

MR. LEMMON: There were cash purchases, yes.

COMMISSIONER LEMAN: This was an operation which did not understand that moral suasion was being used -- I am not sure this is what was being done -- by informing you in this case. There certainly was no implication that the government wanted your industry to do anything against its best interests in its own judgment.

MR. BRYDEN: I do not think that this could be called moral suasion, really. I think this was a meeting to put us in the position, the larger buyers in possession of the background and reasons for this operation. I would doubt very much if you would call that meeting at that time anything that would have anything to do with moral suasion as such.

MR. POYNTZ: It was just communication.

MR. BRYDEN: Yes, and I think very effectively done at that time.

COMMISSIONER LEMAN: Well, in the sense that it was not moral suasion, what about communication by means of a sort of open mouth policy as to what the

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COMMISSIONER LEMAN: Well, in the sense that it was not moral suasion, what about communication by means of a sort of open mouth policy as to what the

objectives are and why would this sort of thing have to be done in private?

MR. BRYDEN: Well, I do not think you want open mouth policy, as you put it, under normal operating circumstances. This was a special operation and it was a very desirable one, but in the normal matter of events I do not think you would need to go that far to develop your communications. I think this is the sort of thing that should happen under special situations.

COMMISSIONER GIBSON: There is a point I would like to raise, Mr. Chairman, in this regard. You say in the exercise of moral suasion -- I think it is better to call it persuasion here -- that the central bank should not ask anybody to operate in a manner that is against its own interests. Now, this brings up the very difficult problem of timing. It is a question of how you judge your own interests. If you take the long view today you would agree with them; if you took the short view today it is against your interests. When somebody tries to convince you to do something you were not otherwise going to do, then in fact you are being asked to do something which you thought at that immediate point not in your own interests. I suggest that persuasion or moral suasion is asking you something just at that particular moment which you would not otherwise have done. Is this a reasonable explanation?

MR. BRYDEN: Yes, using moral suasion in that sense I think that is probably true. In the sense we were talking about in the conversion loan, I

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MR. BRYDEN: Yes, using moral suasion in that sense I think that is probably true. In the [illegible]

think it was, perhaps, communication. There was no pressure brought on us to do anything. It was communication to us and subsequently we made up our own minds having regard to the total operations, the context in which we would convert the existing bonds, whether you bought additional bonds for cash or what have you. I do not think that could be termed moral suasion in any sense.

COMMISSIONER GIBSON: I think that is a different case but you say in your brief that there are times when you think the central bank should use moral suasion, rather emergency times, the suggestion is, but you qualify this by saying that people should never be asked to do things -- in your own testimony, to do things that are against their own interests.
I wonder if this really stands up?

MR. BRYDEN: Can you give me the reference in the brief?

COMMISSIONER LEMAN: Page 98.

MR. BRYDEN: I still do not quite see where we said that moral suasion was a good thing.

COMMISSIONER MACKINTOSH: It must be if it is moral.

THE CHAIRMAN: What I am trying to figure out is what has the "moral" got to do with it no matter how you look at it?

COMMISSIONER GIBSON: I am sure somewhere you say there are times when moral suasion should be used or could be used. But you know your brief and if you did not say it that is not the case.

THE CHAIRMAN: I thought I saw it some place.

MR. BRYDEN: I think on page 97 we start a discussion of persuasion and discussion. We made the point that discussions take place with the chartered bankers at fairly regular intervals with money market dealers and others of the financial community from time to time, that some of these were initiated by the banks and some by interested groups and we feel that discussions of this sort and a free exchange of views cannot help but be constructive and build confidence each in the other.

Then, paragraph 6.35 relates our own special instance where we have had that type of discussion. We refer to the war time period. We refer also to once having a discussion in 1951 on the subject of inflation. We also mention, I think, that conversion loan operation. We mention discussions which produced eventually the statistics of the purchases and sales of the twelve large companies and this is concluded by saying that these meetings and discussions were an effective means of communication and we believed useful at the time and in the context of events, and that they should continue to be contemplated when matters of importance arise and we believe that they are most effective when conducted without any undue publicity. I am having a little problem with this persuasion thing here.

THE CHAIRMAN: I think the expression must have been in the Investment Dealers brief.

COMMISSIONER GIBSON: Possibly. You were talking about this question of moral suasion and you

MR. BRYDEN: I think on page 97 we start a [illegible] of persuasion and discussion. We make the point that discussions take place with the chartered bankers at fairly regular intervals with money market dealers and others of the financial community from time to time, that some of these were initiated by the banks and some by interested groups and we feel that discussions of this sort and a free exchange of views cannot help but be constructive and build confidence each in the other.

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seemed to think that there were circumstances when you should use this approach and you qualified it by saying that people should not be asked to do anything against their interests. This is the problem that bothers me, that you say that people should not be asked to do anything against their interests and then say this should be continued.

MR. HOLMES: I think it means we should be free to use it.

MR. POYNTZ: I think on the question of semantics Mr. Gibson is right, that if there is need for persuasion you are going against somebody's judgment, some preconceived judgment, anyway.

MR. RIEDER: On the other hand, there will be times when what is good for the country is good for us as an industry and perhaps we have to be persuaded to that effect.

COMMISSIONER GIBSON: It is taking a longer view than you otherwise would have taken.

THE CHAIRMAN: It is in the general public interest which might at the moment conflict with your interest but your interest is in the long run involved with the public's.

MR. POYNTZ: Yes, and the question of the persuasion involves communication. At the same time the communication might alter the judgment of those you are trying to persuade.

THE CHAIRMAN: That is what you are doing every day when people are buying your insurance.

MR. HOLMES: It is all for their own good, though.

MR. BRYDEN: That is what is known as using the close.

COMMISSIONER GIBSON: This same basic problem in the long run versus the short run comes up in your discussion of objectives. In the long run what you say is right, that these various objectives are not really comparable but the long run does not mean very much in terms of real savings and when the actual day to day decisions are made they are frequently in conflict, not always. You are not sure whether they are or whether they are not, but there is very often considerable doubt. With this in mind I would be very interested to know where you would put the emphasis on these various objectives. For instance, at any given time, assuming there is some unemployment and we are not in a strong business situation and regardless of running a deficit, should the deficit be increased. These are the actual kind of decisions you come up against day by day and these are decisions that determine how you get your balance in these matters. I wonder if you would care to comment more directly on this problem.

MR. BRYDEN: Well, it is awfully difficult to make direct comments until you are actually faced with the responsibility of making the decision. It is awfully easy to have views from the outside. Again it seems to me that particularly those two objectives

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we have been talking about, there are times when one should be uppermost and there are other times when the other one should be uppermost. You cited a situation where we have some degree of unemployment, not a very robust business situation, et cetera. It is the point at which you would try, it seems to me, to bring the whole arsenal of weapons to avoid or cushion the recession. Each recession is different. Your policy at that point is probably going to be your best judgment as to what is going to improve the situation.

As that starts to head out, then I think at some point price stability becomes uppermost and again you have to pull in as many weapons as you can and give careful emphasis to the maintenance of price stability. At some point we cut down again and I sort of visualize this as a veering towards these two sort of parallel objectives, if you will, and the decisions are difficult.

COMMISSIONER GIBSON: Let us put it more specifically. Supposing in the process of taking out the arsenal, or if you reached a point where business is very good and that this involves running deficits which concern the buyers of bonds and maybe even foreigners about our currency, then what do you do?

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In the short run, as we all know, these things can be very much in conflict.

MR. BRYDEN: I think that you have to do your best to operate your way through these imbalanced situations. You are not always going to be able to do it without getting hurt because it does seem that at times you get into a position where you have expectations, or have had them, or you have got a standard of living which you cannot maintain from your own resources. True, you hit these down periods such as I think we are in now, for example. I am not sure at all that we can get back into balance without some stresses and strains at least in various areas of the economy. I think you have to take them in order to once again get yourself a little more on side, if you will, with your balance of payments. You certainly have to take what steps you can to improve your unemployment situation. Inflation is rarely a problem at the point at which you have unused plant capacity, but as soon as your situation starts to tighten up I think your emphasis have to shift over to the other end of it.

The perverse portion of it is that underlying the whole thing is the matter of confidence on the part of investors and others; confidence that the situation is in balance. I think that that confidence sort of declined within recent months for what you could consider fairly obvious reasons looking back at this point. As soon as you have any erosion of confidence, I do not think the reactions of

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other individuals, particularly foreigners, to our situation follows the normal pattern. There is a sort of scare element enters into it, and that could reasonably well be part of the reason why we at the moment do not appear to be as attractive to foreign capital as we have been.

I think that is all a portion of the lack in confidence on the part of foreigners, as far as we are concerned, and it is leading to very significant problems; problems which we are going to have to face to once more get ourselves back in the position where we are relying on our own efforts, because I think it is true that no other countries in the world owe us a living. We have to make our living for ourselves.

MR. HOLMES: I do not know anything about these finer elements of adjustment from time to time, but I should like to say that very definitely I do not think a solution to our problems comes from a continuing government deficit, or can come from a continued government deficit. If you have unemployment problems or problems relating to stability of currency and you cannot see your way clear to rid yourself of continuing governments you are in trouble continually.

COMMISSIONER GIBSON: In other words, you put high priority on the value of the currency?

MR. HOLMES: I put quite high priority on the value of the currency, and I do not think that other problem is solved by definite inflationary policies.

COMMISSIONER BROWN: You have doubt as to the efficacy of monetary policy?

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MR. HOLMES: We have had inflation really for about 30 years and we now end up with a fairly high degree of unemployment.

THE CHAIRMAN: Yes, but during a great part of that time we had a reasonable high degree of employment.

MR. HOLMES: Yes, but what is the solution; another 30 years of inflation?

COMMISSIONER BROWN: This gets back to the point that you have no confidence in monetary policy as an instrument?

MR. HOLMES: Well, no, I would not say that, but I think you have got to get very much nearer to a balanced budget before you can adjust back and forth. You are in a position now where every time you try to cure unemployment or lowered business you just add to the deficit.

COMMISSIONER BROWN: Putting it this other way, you have greater confidence in monetary policy to slow things down than its effectiveness in making things better?

MR. HOLMES: No, I would not say that, either, but you are in a position now where you have not any leeway; you can only move one way.

MR. BRYDEN: I think, Mr. Chairman, that monetary policy is a flexible instrument; it is of general application; it is extremely useful, but it is not a wonder cure for everything because to me monetary policy cannot make up for too many unbalanced budgets; too burdensome or inequitable taxation. It

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COMMISSIONER BROWN: What I was trying to get at was that Mr. Holmes's opinion of the current situation is apparently one that cannot be resolved, or at least he does not think the unemployment situation can be resolved by monetary and fiscal policies.

MR. HOLMES: No, I do not quite agree when you say monetary and fiscal policies. It certainly cannot be resolved by monetary policies at the present.

COMMISSIONER BROWN: Well, what sort of fiscal policies would you think should go into effect to resolve the unemployment situation?

MR. HOLMES: Well, I think you have in one way or another to reduce your government deficits so that you are in a position to use policies to encourage business improvement, or to cool it off.

COMMISSIONER BROWN: Your thought is that you have got yourself strapped into a situation where the first move is to re-establish confidence?

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some way to re-establish a balance. You must have control of the situation.

COMMISSIONER BROWN: Have you any comment to make about that, Mr. Bryden?

MR. BRYDEN: As to what we should do currently?

COMMISSIONER BROWN: Yes, all right, what should we do currently?

MR. McCARTHY: I would think, Mr. Brown, if there is a man in this country that can give you an answer to that question he has a public duty to come forward and tell us about it.

COMMISSIONER BROWN: I am trying to find out.

COMMISSIONER LEMAN: I would like to ask a couple of questions in respect to the pension fund area and segregated fund area.

Basically would you say that the introduction of this segregated fund legislation would mean that insurance companies are pretty well being used as administrators of the investment management for the fund much like a trust company would be? That is about it, is it?

MR. TUCK: We still must issue insurance contracts.

COMMISSIONER LEMAN: Must there be an insurance element connected with it?

MR. LEMMON: There must be, yes.

COMMISSIONER LEMAN: But the insurance element is not an important one in that case? I under-

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stood yesterday during the brief reference we had to these funds that this was a case where your investment policies would be, shall I call it, much more liberal than with regard to your insurance reserves. What is the insurance element with regard to these segregated funds?

MR. TUCK: Mr. Leman, the statute refers to two kinds of life insurance, using that in the broad sense of the term, under which the segregated fund technique could be applied. One is equities and the second is insurance providing for the establishment of accumulation and payments for certain things, but the word "insurance" precedes all these other things, so that our understanding is that companies must include in their contracts that are backed up by these segregated funds some form of insurance such as a guarantee of the mortality rate on the annuities that emerge or a guarantee of the annuity rates themselves. The thing that is flexible in the segregated funds is the investment that can be used to back it up. That is the essential difference from the segregated funds and our guarantee business. The quantitative restrictions do not apply, nor do the real estate restrictions.

COMMISSIONER LEMAN: Would the act prohibit you now from acting just like say a trustee in managing a pension fund?

MR. TUCK: We cannot be a bare trustee.

COMMISSIONER LEMAN: I wonder if the trusteeship element is absolutely essential. If a corporation went to you tomorrow and said: we would like to organize

a pension fund for our employees to which we will contribute and to which the employees will contribute and you are going to manage it for us and make the investments for us, would you necessarily be a trustee unless the instrument creating it makes you a trustee?

MR. TUCK: We would not be a trustee. We would be held pursuant to the contract to relations between parties to an ordinary contract.

COMMISSIONER LEMAN: You could do that? There is nothing in the law that prevents you from doing that?

MR. TUCK: That is how we would do it. We cannot get ourselves in the position of being a trustee in the legal sense of that word.

COMMISSIONER LEMAN: This is not a business that has been entered into by insurance companies, is it?

MR. TUCK: Well, the machinery for using these segregated funds was only inserted in the act a couple of years ago -- less than that, a year ago March.

MR. RIEDER: We could do what you suggest, I understand, but we would also have to guarantee some annuity rates to be used with that money at retirement age and that is where the mortality element or insurance element comes in. A trust company cannot do that.

COMMISSIONER BROWN: You do not guarantee what the fund is going to amount to at age 70 but you guarantee what annuity you will provide for each dollar that is then available, is that the point?

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MR. BRYDEN: That is the point. In fact, in respect to pension plans we offer the facility of the investment of some portion of the plan in equities. We do not guarantee in any shape or form what that equity portion will amount to. We do, however, guarantee reconversion, if you will, from the equity into actual annuities at specific rates.

COMMISSIONER BROWN: Even though the doctors come up with something so that people can live for 150 years, you guarantee this?

MR. BRYDEN: It is guaranteed as of now. We would be sorry if that happened.

MR. LEMMON: Individually or collectively?

MR. BRYDEN: I could not care less.

MR. RIEDER: We have both sides of that; we have the insurance and annuities.

COMMISSIONER BROWN: I expected somebody to bring that up.

COMMISSIONER LEMAN: In relation to this you refer to the government pension scheme and you express some concern about the level at which the universal pension has reached. We will talk about it some more. How would you measure what is the proper point at which this ought to stop?

MR. BRYDEN: Mr. Holmes would you like to talk about that second debt position?

MR. HOLMES: I think the level is determined by what you are prepared to pay for it without taxing yourself so heavily that you affect your growth and the

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I think also you have to be sure you know that you are paying for them. That is one objection we have to the second debt type of loans in the United States, because they are promising things that they are not at the moment paying for.

COMMISSIONER LEMAN: They are not funding their liability; their calculated liability?

MR. HOLMES: It is calculated on a funded basis but without funding.

MR. POYNTZ: It is a cross subsidy from one generation to another.

COMMISSIONER LEMAN: Is it basically your philosophy here that these things should be funded as they go along?

MR. HOLMES: Our own basis in this country is quite a sound basis. We pay for it, practically speaking, as we go along. So, if you make $65 a month and can pay for it, that is O.K. You know at once whether you can pay for it or not. At the moment we are not paying for it one way or another, and that is a cinch, but we know what it is and we know what we should pay for it. If we can pay for it, that is fine.

We approve of the basis used in Canada for old age security.

COMMISSIONER LEMAN: I do not see in what sense in Canada the old age pension is being particularly

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COMMISSIONER LEMAN: I do not see in what sense in Canada the old age pension is being particularly

sound, in the sense that it is not funded, is it?

MR. HOLMES: No, I do not think the government can fund a scheme, and that is the difficulty of thinking of a funded scheme for government policies. They cannot do it and never have done it.

In respect to the American scheme there originally was a great debate as to whether it ought to be funded or not. Finally what solved that question was that if they funded it on the original basis it would have been far more than the debt in the United States. They decided not to fund it and to use it as a pay as you go scheme, but it was an improperly devised scheme for a pay as you go scheme because it was not universal and did not go to people of all ages. The result is that at first all they had were contributions with nobody drawing from the fund. It has gone on and is still very largely in that category. That is, the people paying for the fund are not paying for what they are promised in the way of benefits.

COMMISSIONER BROWN: Well, if we look at these various plans and schemes, especially the ones operated in the private sector, you seem to imply that pension funds et cetera are good for the economy. Probably they are if they encourage savings. I suppose that would make them good for the economy, but when you look at the investment side of these funded plans, the type of investments that they have attracted to date -- those that are in the class of what we call trustee investment plans -- in what sense do you think

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gone on and is still very largely in that category.
That is, the people paying for the fund are not paying
for what they are promised in the way of benefits.

COMMISSIONER [illegible]: Well, if we look at
[illegible] plans and [illegible] especially the ones
operated in the private sector, you seem to imply that
pension funds et cetera are good for the economy.

[illegible]
that would make them good for the economy, but when
you look at the investment side of these funded plans,
the type of investments that they have attracted to
date -- those that are in the class of what we call
trustee investment plans -- in what sense do you think

they are so beneficial to the economy if they do not introduce people into risk ventures and that sort of thing?

MR. HOLMES: Well, there are others. I do not feel at all that a loan type of investment is not in the public interest. Without the loan type of investment you would not have the savings of individuals at all. I mean, they would not be able to own their own homes unless there was loanable money, because they do not have that much money at one time. I do not look at the risk type of investment as being superior to the loan type of investment. It is the balance that you want. There are certain people that want to take a risk but they want to borrow the money from somebody else to carry it through. There are risk takers who have become millionaires since the war borrowing life insurance company money, but who built the houses, the risk taker or the companies? I do not know. I do not think there is one section of capital that is definitely more superior to another.

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COMMISSIONER LEMAN: What is important is what areas does the capital go to, whether in the form of loans or equities and distinguishing between loans or equities or distinguishing between the areas in which the funds are invested.

MR. HOLMES: It gets into practically all areas in the country, I would think, through life insurance companies. It gets into mortgages, both industrial and residential. It gets into corporate bonds and it gets into every area, into the development of the country.

COMMISSIONER LEMAN: Well, we reviewed yesterday the restrictions on the investment powers, and there are restrictions on investment powers of trustees in the places where there is trustee legislation and they are of a restricted character. Are they not a little bit of this rigidity?

MR. BRYDEN: Don't we have to think, at least partly, in terms of why these particular funds exist. After all, they are savings by people who are members of the plan with a view to having a pension at the point at which they retire.

Now, to a very great measure the money that goes in is a somewhat involuntary saving, if you will, in the sense that if you are a member there is a certain prescribed contribution that you must make, that they do produce rather large pools of private capital which is available for use in the capital market and through it for the development of the country, but the primary duty of these particular pools

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is to produce at the retirement period that pension.

Now, to what extent you could expect pools of that kind and with that end purpose in view to be invested in very new and high risk enterprises is an open question. The mortality in that particular field of investment is high and it requires a fair amount of money per investment to get into it even now.

I suppose that if you had 30 ventures, new business ventures, if you had two that really turned out, that might be as much as you might expect. You would probably have another group which just didn't make it and that is why diversification of risk within that area is important, but I do think it is pretty debateable to what extent pension fund monies as such should be used for that purpose.

There are other monies available -- not in pension funds -- and which can be used in moderation for that purpose. There also is money in the country that you know of that is constantly on the lookout for the financing of new business ventures. From my experience, some of that exists but doesn't seem to be being used.

COMMISSIONER LEMAN: Well, why would you think that is?

MR. BRYDEN: I guess that there are not enough new business ventures which the managers of that particular capital think sufficiently attractive to finance.

COMMISSIONER LEMAN: And yet we have the I.D.B. created and we have had requests from various

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COMMISSIONER LEMAN: And yet we have the I.D.B. created and we have had requests from various

development banking has satisfied some measure of it, but how you get to the point that you can satisfy all, I don't know.

MR. POYNTZ: I don't believe you can make a good case for filling up the gap that exists because of the riskiness of a venture with a man's pension fund money.

MR. HOLMES: It must offer a credit if your pension fund money is used. That doesn't say that you can't take considerable risk providing the return on successful ventures is sufficient to pay for the risk on the unsuccessful ones.

Whether life insurance companies are entirely suitable for that sort of operation is very questionable, although we are venturing into some of what was described this morning. I think we are sympathetic to trying to get into that, but it is a different type of organization because the risk venture usually depends so much on the personality and the ability of the one man who is operating it and it is a difficult thing for an organization to assess the ability of the man.

THE CHAIRMAN: Thank you very much gentlemen; you made a very valuable contribution to our studies in the field that has been assigned to us, and we thank you very much.

It may be that in the next few weeks the staff may be in touch with you for further information if there is anything that occurs to us.

MR. BRYDEN: We shall be most happy to

co-operate in any way we can.

THE CHAIRMAN: We will now adjourn until 8.45 tomorrow morning, when we shall hear the submission of the Investment Dealers' Association.

MR. RIEDER: Mr. Chairman, I personally have not had very much to say at this meeting, but some of my colleagues have, and if we have been of assistance to you in your job we are more than happy.

--- Adjournment at 12.35 P.M.

Royal Commission on Banking and Finance

Hearings held at

Ottawa

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SECTION 1

INTRODUCTION

1.1 The Canadian Life Insurance Officers Association is a voluntary organisation consisting of 100 companies in the life insurance business in Canada. These companies had $50 billion of life insurance in force in Canada in 1961. This represents 99 per cent of the total life insurance (excluding fraternal benefit insurance) owned by nearly 9 million Canadians. The life insurance companies have more than $8½ billion invested in Canada on behalf of their policyholders and they are currently investing or reinvesting about $1¾ billion each year.

1.2 The terms of reference of the Royal Commission on Banking and Finance are to:

> "enquire into and report upon the structure and methods of operation of the Canadian financial system, including the banking and monetary system and the institutions and processes involved in the flow of funds through the capital market."

The life insurance companies are keenly interested in the Commission's deliberations and studies. They believe that a review of Canada's financial system is important and timely and hope that the information and views set forth in this submission will prove to be a constructive contribution to this review.

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[illegible]

[illegible]

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1.3 The Association provides a forum for the [illegible]

industry. It operates only by making recommendations to its member companies which they are free to accept or reject. A list of member companies of this Association is appended together with the names of the members of the Special Committee responsible for the preparation of the submission.

1.4 Life Insurance is transacted in Canada by companies registered under federal insurance laws, by additional companies operating under provincial charters without federal registry, and by fraternal benefit societies. This submission relates only to the life insurance companies. Statistics on the operations of provincial companies are not as readily available as on federally-registered companies but are included wherever possible.

SECTION 2

SUMMARY AND OBSERVATIONS

2.1 At the end of 1960, more than $8\frac{1}{2}$ million Canadians owned $47 billion of life insurance. This represented an average of $10,400 per household. Canadians also had in force with the life insurance companies more than 649,000 annuity certificates providing for present and future annual payments of $736 million a year. In addition, 5 million Canadians had some form of health insurance coverage provided by life insurance companies. (Paras. 3.15-3.28)

2.2. Life insurance was provided in Canada by 121 life insurance companies at the end of 1960. The number had expanded by more than 50 per cent in the preceding 25 years. Ninety-nine of these companies were registered with the federal Department of Insurance and 22 with provincial Departments only. Of the 121 companies, 58 were classified as Canadian while 63 were of external origin. Of the 58 Canadian companies, 20 were mutual, 5 were in the process of becoming mutual and 33 were companies with share capital. (Paras. 3.1-3.9)

2.3 The controlling stock interest in 12 of the 58 Canadian companies lies outside Canada. In the case of 7 of these, control has passed out of Canada since 1954. Permission to mutualize, that is to purchase their own shares, granted to stock companies in 1957, may have prevented further acquisitions of this kind. The Commission might consider, however, whether the prohibition in the Insurance Acts against the investing of Canadian life insurance funds in the shares of another

life company may not have militated against the retention of ownership of Canadian life insurance companies in Canada. (Paras. 3.10-3.14)

2.4 Fourteen of the Canadian companies do business outside of Canada. The $13 billion of life insurance these companies have in force abroad equals 42 per cent of their total business. Of this business outside of Canada, 70 per cent is on the lives of policyholders in the United States, 16 per cent on persons in the British Isles, 2 per cent on Asians, 6 per cent on Africans and 6 per cent on persons in the Caribbean area and Latin America. Non-resident companies doing business here have about $14 billion of life insurance in force on Canadians. (Paras. 3.3 and 3.4)

2.5 The life insurance industry has been one of the prime financial intermediaries in the Canadian financial system for more than 100 years. In recent years saving through life insurance has averaged about 1.7 per cent of disposable personal income and has amounted to more than 25 per cent of the personal saving of Canadians. Experience has shown that in periods relatively free of extraordinary economic or financial events, annual changes in insurance saving tend to more closely with changes in disposable personal income. Prolonged economic decline, however, has a relatively heavier impact on this form of saving than on disposable personal income while in periods of rapid inflation, with income rising, the increase in life insurance saving tends to respond more slowly. (Paras. 4.1-4.8)

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premium plans of life insurance is the basis for the accumulation of funds in the companies. Level-premium plans require the accumulation of a reserve during their early years to meet the rising level of claims that will occur during the later years. Although there has been in recent years a great growth in group insurance, which is almost always term insurance, and a rising proportion of term insurance in the sale of individual policies, the purchase of level premium "permanent" plans has increased in absolute amounts. In addition, an increasing proportion of saving has been done in the form of annuities. (Paras. 3.33-3.40)

2.7 The federal and provincial governments have shared responsibility for supervision of the insurance business in Canada since 1868. Briefly, for federally-registered companies the federal Department of Insurance concerns itself with the solvency of insurers and the provincial Departments with the regulations of the business. For some provincial companies provincial Departments assume both responsibilities. By and large, insurance legislation and government regulation have been well conceived and well administered in Canada. As new forms of investments, new types of policies and new problems have developed, amendments to the legislation have been sought and many have been enacted. (Paras. 3.44-3.47)

2.8 Saving through life insurance had resulted in the gradual accumulation of more than $8.2 billion in assets held on behalf of Canadian policyholders and annuitants at the end of 1960. In addition, assets

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relating to the life companies' health insurance business amounted to about $80 million. The assets held outside of Canada by Canadian companies on behalf of their external business amounted to $2.8 billion. At the same time assets held in Canada by non-resident companies for the protection of Canadian policyholders amounted to $2.3 billion. (Paras. 3.41-3.42; 4.23-4.25)

2.9 These assets conform to the provisions of the Insurance Acts. Within the framework there exists ample room for a significant exercise of judgment by individual companies in the conduct of their investment operations and ample room for the life insurance industry to employ its funds through wide diversification, both as to category of asset and geographical area, for the financing of development within the Canadian economy. (Para. 4.14)

2.10 The Insurance Acts define certain broad categories of investment within which life insurance funds may be placed and impose certain additional limitations within some categories. They also define certain investments which are prohibited. The recognition of the trustee nature of these funds, these restrictions have as their main objective the avoidance of undue risk, the limitation of concentration of economic power through stock ownership and the prohibition of loans to directors, officers or their families either directly or through corporations they control. The companies are allowed to have a maximum of 5 per cent of their assets that do not meet the specific

eligibility tests in the Acts. Amendments made in 1961 allow the setting up of segregated funds for policies the reserves on which vary in amount depending on the market value of the assets. In such funds the quantitative limitations on common stock or real estate investment do not apply but the limitation on non-specified investments is retained. (Paras. 4.9-4.17)

2.11 During discussions with the federal authorities prior to the legislative amendments in 1961, two major changes were suggested but not adopted. The first concerns some relaxation in the 15 per cent limit on common stocks and the second a change in the year-end valuation standard. With regard to the first the companies felt that although they currently held much less than 15 per cent of their assets in common stocks, under appropriate market conditions the present limit might be too restrictive. They pointed out that some of the non-resident companies are even now finding the limit restrictive. With regard to the valuation standard it was suggested that amortized values be extended to municipal securities in Canada, the United States and the United Kingdom and that for corporate securities and shares the average of three most recent year-end market values be used. (Paras. 4.18-4.20)

2.12 The introduction of the segregated fund provisions answered much of the problem presented by the 15 per cent common stock limit as far as the Canadian companies were concerned. The suggestion put forward regarding the valuation standard was not a unanimous view. The great majority of the companies

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2.12 The introduction of the segregated fund provisions answered much of the problem presented by the 15 per cent common stock limit as far as the Canadian companies were concerned. The suggestion put forward regarding the valuation standard was not a unanimous view. The great majority of the companies

felt that some further relief from the constraints of year-end market valuation was desirable since any sharp temporary downward shift in market values that resulted in very substantial encroachment on surplus funds tended to produce inequities in the incidence of surplus distribution and led to unwarranted conclusions regarding surplus depletion. On the other hand there is a view that the use of a market value basis is more conducive of an active market policy. The Commission may wish to consider this question in the content of the capital market generally and particularly the market for common stocks. (Paras. 4.20-4.22)

2.13 The investment operations of the insurance companies play a very important role in supplying the capital needs of the Canadian economy. For example, in 1961 the companies' lending approvals for residential mortgage loans of $600 million constituted 44 per cent of all approvals for such loans; lending approvals of $141 million for non-residential mortgages comprised 47 per cent of all institutional approvals; net purchases by the life companies of provincial bonds of $132 million amounted to 14 per cent of all net new issues; net purchases of municipal bonds of $47 million amounted to 18 per cent of all net new municipal issues; and net purchases of corporate and other bonds of $77 million amounted to 38 per cent of all net new issues. However the life companies' increase in policy loans of $15 million amounted to only 5 per cent of the increase in consumer credit outstanding. (Paras. 4.47-4.54)

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2.14 Life insurance companies can only increase their overall investment by the net saving that they are able to attract. However, in addition to the annual increase in assets resulting from the net saving flow, the companies have for re-investment funds arising from the repayments on existing assets - assets which have either been redeemed or reached maturity - and assets which have been sold. The degree of total activity varies significantly as between individual companies but it would appear that gross investments by all companies is about 2 to 2½ times the net increase in assets. This produces a great impact on the capital market than the annual increase in assets suggests.

(Paras. 4.32-4.44)

2.15 The theory of life insurance investment is based on the nature of the liabilities assumed - the commitment to pay claims and benefits as they become due and the interest guarantees given on the moneys already received and to be received in the future. Life insurance protection must be absolutely reliable.

(Paras.5.1-5.3)

2.16 Safety of principal is the first consideration. Life insurance funds must be invested in such a way that risk of loss is minimized. This is accomplished by careful selection of individual investments as to their credit-worthiness, that is, the ability to pay interest and to repay principal when due, and by widespread diversification of risk through investment in different categories of assets and in different geographical areas.

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2.17 The second consideration is the investment of funds to yield as large an interest return as possible consistent with the required safety, so that the cost of insurance to policyholders may be as low as possible. For this reason, the life insurance companies are extremely sensitive to yields obtainable in the capital market. (Para. 5.5)

2.18 The diversification of life insurance assets held in Canada at the end of 1960 by category of asset was as follows: bonds 48.4 per cent, stocks 3.1 per cent, mortgages 37.6 per cent, real estate 3.6 per cent, policy loans 4.3 per cent and other assets 3.0 per cent. These, of course, are average figures and do not indicate the significant degree of deviation in the investment policy of individual companies. For example, among Canadian companies, bonds accounted for from 97 per cent to 26 per cent of invested assets, stocks from 12 per cent to nil, mortgages from 64 per cent to nil and real estate from 10 per cent to nil. (Paras. 4.25-4.31; 5.45-5.52)

2.19 The diversification obtained by geographical area diffuses life insurance assets widely throughout the economy. Although life insurance companies are national concerns and policyholders look to the entire pool of assets for their security, the regional distribution of assets is quite close to the regional distribution of their liabilities. The assets and liabilities will change from year to year as assets respond to the availability of investments and the liabilities to both new business and the aging of existing business. (Paras.5.22-5.26)

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2.20 The effect of monetary policy on the investment practice of the life insurance companies flows essentially from changing interest rate levels and relationships. The spectrum of investment is wide and, thus, has many exposures to changing interest rates. (Paras. 5.34-5.35)

2.21 Life insurance companies are responsive to change or expectation of near-term change in interest rate levels in at least four ways: (a) the direction of the investment flow; (b) the liquidity of existing assets; (c) the generation of cash for investment; and (d)the degree of forward commitments.

(Paras. 5.36-5.41)

2.22 Most life insurance companies are desirous of assuming a minimum of exchange rate risk in their investment operations. In general, the attempt is made to match foreign currency assets to foreign currency liabilities. In some countries this is virtually a requirement. Some companies have been prepared, however, to accept some exchange risk from time to time. (Paras. 5.42-5.44)

2.23 There has been a steady upward trend in both the gross and net rates of interest earned over the last 10 years. In varying degrees this has applied to all categories of asset. Investment expense as a per cent of assets has decreased.

(Paras. 5.53-5.55)

2.24 The distribution of assets by category for Canadian and United States companies is not significantly different. Comparison with the United Kingdom companies,

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however, shows that the latter place more emphasis on common stocks and real estate and less on mortgages. The reason would appear to be three-fold:

(a) In the United Kingdom there is almost a complete lack of restriction on the powers of investment and although at the year-end stock exchange securities are usually taken at market values, and other assets at cost, the companies' actuaries have much more freedom in varying the interest rate basis of accumulation for the actuarial reserves.

(b) In the United Kingdom guaranteed cash values are not universally available as they are on this continent. This allows greater freedom in valuation. The practice of disbursing dividends in the form of reversionary additions to the sum assured allows the funds built up for this purpose to form a cushion against any temporary recession in market values.

(c) In the United Kingdom mortgages are regarded as relatively short-term and yields are not so attractive, thus forcing insurance funds into equities and real estate.

(Paras. 5.61-5.62;
5.69-5.83)

2,25 The life insurance companies in Canada make exhaustive reports to the Superintendents of Insurance each year. These are summarized and published by the

Superintendents. Companies, of course, present statements of their own affairs at annual meetings. At least once each year the premium notices or receipts of Canadian federally-registered companies must contain a statement of the participating policyholders' right to attend and to vote in person or by proxy at such meetings. (Paras. 3.49-3.50)

2.26 The life insurance business is a complicated business involving as it does so many forward judgments relative to mortality , interest and expense. Comparison as between companies requires exhaustive and competent analysis. No easy and satisfactory method has yet been found to produce a simple index or indices for comparative purposes. Comparison of premium levels, dividends and cash surrender values for strictly comparable policies in different companies affords the easiest and best method but even it can only be used with some qualification. Strictly comparable policies are difficult to find and any comparison of this nature may fail to take into account important policy provisions. Important considerations such as service and dividend distribution policy lie beyond the scope of mechanistic comparison. (Paras. 3.51-3.54)

2.27 The Association believes that there is the highest need for a unification of monetary, fiscal, debt-management and exchange rate policies. When they are co-ordinated, each derives strength from the others. When not co-ordinated, no one policy, and particularly monetary policy, can in the long run make up for shortcomings in the other policies. (Paras.6.5-6.8)

2.28 The harmony and co-ordination to be desired in financial policy leads to the conclusion that government must accept ultimate responsibility for monetary policy. The initiation and implementation of monetary policy, however, should be the responsibility of the Bank of Canada and it should be accorded wide latitude until such time as the views of government and the Governor cannot be reconciled, at which time government views should be set forth in a directive. If the Governor cannot accept such directive, he should feel called upon to resign, thus bringing such differences to public attention. Such a brake on any possible abuse of the machinery of credit creation for political ends is a necessary safeguard. The Association suggests that the Bank of Canada Act be amended to make this position abundantly clear. (Paras. 6.9-6.11)

2.29 The Association believes that the Bank of Canada should seek to carry out its monetary policy by varying the money supply, thus changing interest levels and influencing liquidity. In this way the Bank should seek through a responsive capital market to augment or dampen the rate of economic growth, contribute to price stability and act as a balance wheel in regulating economic progress. (Paras. 6.12-6.13)

2.30 The Association believes, however, that there is an important limitation to domestically-initiated changes in interest rate levels in the degree to which the Canadian capital market is oriented to that of United States. Beyond certain limits, changes in interest rate levels may cause an undesirable flow of

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short-term funds across the border and affect the balance of payments. (Para. 6.14)

2.31 The Association believes that if the operations of the capital market from time to time lead to distortion or an uneven or undesirable flow of funds to ultimate users and correctives are deemed to be necessary, the problem should be tackled directly by government through temporary regulations rather than by attempting to bring non-bank financial intermediaries under some form of continuing relationship with the central bank. (Para. 6.12)

2.32 The Association feels, however, that in peace-time at least, there is rarely a case for the extension of direct controls throughout the economy and that they should be considered only as a last resort. Excesses of a character that need to be controlled by this means are invariably only symptoms of a deep-seated maladjustment. They may temporarily alleviate the symptoms but do little to cure the disease and it is the disease that is important. Direct controls also require extensive regulations and enforcement officers to curb pressures and evasions. (Paras. 6.22-6.24)

2.33 Difficulties that may be experienced from time to time by certain borrowers or classes of borrowers in obtaining funds through the capital market at what they may consider to be reasonable interest rates usually lead to the suggestion that governmental authority should impose, by legislation or otherwise, restrictions whereby financial intermediaries would be required to invest a certain proportion of their funds in certain categories

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of investment. The Association believes that such suggestions are not in the best interest of either policyholders or the nation. (Para. 6.25)

2.34 There never is a time when all borrowing "needs" can be met from the accrued and accruing savings of the nation. One of the functions of the capital market is to establish priorities. This method may have its imperfections but it has never been proven that the substitution of government direction for the multitude of decisions in the market-place would result in a more effective allocation. (Paras. 6.26-6.27)

2.35 For example, the life insurance companies can only invest the funds they are able to attract. The wide diversification of investment which they have achieved has been illustrated. Any regulations as to minimum proportions in any one category of asset must reduce the amount of funds that can be made available for other purposes. Direction of this kind is almost certain to lower arbitrarily the investment returns of those particular savers who choose to save through life insurance. In the long run, such direction would affect the life insurance companies in their competition for savings. In face, once introduced, the danger would be that the direction would be gradually increased and extended to the point where the personal savings of policyholders would be under government control.

(Paras. 6.28-6.29)

2.36 The Association believes that monetary policy to be effective must operate against a background of confidence - confidence in government policy in all

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its aspects and confidence in reasonable stability in the level of prices. Lack of confidence can stulify the best efforts of monetary management by making the market unresponsive to the changes it desires to bring about. Confidence is enhanced by public understanding, but the Association feels that statements by the Bank of Canada should be confined to considerations of monetary policy and its implementation. The Bank, in the Association,s view, should give the fullest public explanation of what it has done, should keep its emerging views and intent constantly before its responsible Minister but other than that it should be able to pursue its objectives in reasonable anonymity.

(Paras. 6.30-6.33)

2.37 The Association finds it difficult to believe that there is any great matter of principle involved in the discussion concerning the relative merits of the floating re-discount rate and the stated re-discount rate. It suggests that the treatment of the rate is essentially an operating procedure and that it should be possible for the question to be resolved to the satisfaction of the central bank, the chartered banks and the financial community and removed as a bone of contention. To the extent that changes in the re-discount rate can be made meaningful in terms of signalling changes in the direction of monetary policy so much the better. (Para. 6.37)

2.38 The maintenance of price stability or the avoidance of inflation is not only of prime importance to life insurance policyholders in safeguarding the values

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of their policies and the companies' control of operating costs on their behalf but also to all citizens who are beginning to realize that inflation can wipe out their savings just as effectively as prolonged unemployment. (Paras. 6.38-6.41)

2.39 The problem of inflation arises from an imbalance in our economic affairs. Although it manifests itself as a monetary phenomenon in the sense of rising prices, its roots lie much deeper. No ready cure is available. Just as combatting recession requires the use of a broad arsenal of weapons, so combatting inflation requires an equally broad attack, not only on the monetary front, but also in fiscal matters and in economic policy generally. (Para. 6.42)

2.40 The first prerequisite is a determination on the part of government to place reasonable price stability along with a high level of employment and income as the two major objectives of public policy. The second prerequisite should be a willingness to use all paths which will advance the economy toward that goal. Monetary policy, although in the forefront of restraint at these times, needs powerful support from fiscal policy and from the public generally.

(Paras 6.43-6.44)

2.41 With relation to fiscal policy, the Association is concerned about the substantial commitments that governments have already made in the welfare area and with suggestions for further increases. The proportion of national production used for these purposes has risen greatly in the post-war years.

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In particular, the Association is concerned about suggestions that an additional compulsory pension plan should be added to the present universal, flat benefit Old Age Security plan. (Paras. 6.46 and 6.53)

2.42 The present Old Age Security plan was established in 1952 with the support of all political parties and many other interested groups including the life insurance companies. This plan has many advantages. Because it pays the same benefit to everyone aged 70 and over, it proportionately helps most of the lower earners whose need is greatest. It is simple and inexpensive to administer. Increases in benefit have been made on three occasions and the increase immediately reflected in payments to the recipients. The present $65 a month benefit is more generous relative to income than the average benefit to the aged provided under the United States Social Security programme. If money is available for further increases in welfare benefits, the Association feels that first priority should be given to such groups as those unable to work because of permanent disability and widows with dependent children by extending to them the advantages of flat, uniform, basic benefits as a matter of right.

(Paras. 6.47-6.52 and 6.59)

2.43 The Association is opposed to the addition of a government-operated plan providing for graduated benefits on top of our present Old Age Security plan. No government plan of which we are aware, including the United States plan, equates an individual's benefits

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2.43 The Association is opposed to the addition of a government-operated plan providing for graduated benefits on top of our present Old Age Security plan. No government plan of which we are aware, including the United States plan, equates an individual's benefit

to his contributions. Even if it tried to do so, irresistible pressures would arise to borrow from the funds required for future benefit payments in order to make current payments. This transfers heavy costs to future generations. (Paras. 6.55-6.58)

2.44 The continued use of existing pension facilities, subject to minimum requirements of "portability" and benefit level, would avoid the weaknesses inherent in a government-operated plan and would ensure that fund would be accumulated for each contributor from which to pay the benefits promised to him. The investment of these funds would continue to be available to finance Canada's growing economy.

(Paras. 6.60-6.61)

2.45 The capital market in Canada has been growing and is becoming more fully developed over the years. The Association feels that the market today, under normal circumstances, is reasonably responsive to changing supply-demand relationships and is sufficiently broad, sufficiently flexible and sufficiently cohesive to allow monetary policy to be reasonably effective.

(Paras. 7.1 and 7.5)

2.46 The development of a capital market is basically an evolutionary process. This development is aided if the market contains as few barriers or hindrances as possible to the free flow of funds, thus allowing the greatest freedom for interest rates to reflect the changing pressures of supply and demand.

(Paras. 7.2-7.4)

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(Paras. 7.2-7.3)

2.47 Although the Association feels that generally

its members are well served by the existing machinery of the market, it would offer the following observations:

(a) The present size of the bond market is such that the companies believe that neither the services of the so-called bond jobber nor the formation of a bond exchange would be particularly useful. (Paras. 7.7-7.9)

(b) A prime objective of the investment dealer should be the prompt and full distribution of a new issue. Many companies in the Association's membership have difficulty from time to time in getting as large a participation as they might wish in the first instance. They suggest the provision of earlier information concerning a new issue and a prompt delivery date would assist in early and complete distribution.
(Para. 7.1o)

(c) The life insurance companies have long been substantial buyers of bonds of credit-worthy municipalities. The fact that many smaller municipalities are not too well-known seems to limit them in obtaining funds. To the extent that municipal governments cannot borrow directly, it is suggested that some form of pooling arrangement through provincial sponsorship is the only effective way of adding the additional credit to allow access to the capital market. Care must be exercised, however, to ensure that such sponsorship through

the provision of easier credit does not lead to the accumulation of municipal debts that will prove burdensome to repay.

(Para. 7.11)

(d) Small, new and high-risk companies have difficulty in raising both debt and equity capital. Their obligations or shares are far from investment grade. The financing of such new businesses today requires an amount of money that few investors can afford to place on one risk. Privately-financed development corporations participated in by large groups of investors might be a practical way of surmounting this difficulty. It would allow a spread of risk through group participation that would be impossible of attainment by any one investor. Such a development corporation might provide both debt and equity capital and assist in the provision of counsel.

(Paras. 7.12-7.16)

(e) The further development of a secondary mortgage market which would broaden the band of investors interested in mortgages and increase the liquidity of mortgage investments would be desirable. The successive sale of blocks of N.H.A. mortgages by Central Mortgage and Housing Corporation is helping to create this. In Canada, however, it is difficult as yet to visualize enough activity to create a full-fledged secondary mortgage

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(Paras. 7.[illegible]-7.16)

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marketing system. The mortgage departments of the banks, and trust and loan companies seem to offer the best immediate facilities, further strengthened in the long run by the development of a mortgage banking system similar to that in the United States.

(Paras. 7.17-7.25)

(f) There have been suggestions over the years that N.H.A. mortgage insurance be made to apply to loans on existing houses. It is said that this would broaden the market for new houses, bring about a more economic use of existing space and reduce the need for second mortgage financing. On the other hand, it could result in less money being available from private sources for new homes, raise the price of existing houses and monetize a large volume of past savings and appreciation in values, and open the way for a considerable volume of dissaving. If such a course were to be considered, it would be essential, in the Association's view, that the insured mortgage be limited to a bona fide purchaser of a single house who intends to reside in it and the loan limited to, say, 80 per cent of a lending value and subject to an amortization period that recognizes fully the age of the house, its location and its remaining economic life.

(Paras. 7.26-7.27)

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(Paras. 7.26-7.27)

2.48 Years ago it was deemed desirable to place restrictions on the investments of life insurance companies and to supervise their activities in the public interest. The life insurance companies compete with other collectors of savings, particularly in the area of individual and group retirement plans.

(Paras. 7.39-7.42)

2.49 The Association feels that uninsured pension plans are equally long-term and that their activities and particularly their continued solvency is equally important and that they should be brought under government supervision of a somewhat similar character and purpose. They believe, too, that all investment vehicles through which individual accumulation under "registered retirement savings plans" takes place should be the subject of some minimum standards of government supervision. (Para. 7.43)

2.50 The Association believes that the conditions which will allow the life insurance companies to make a maximum contribution toward the accumulation of savings and their constructive employment in the Canadian economy are:

(a) Reasonable stability in the purchasing of the dollar and the preservation of savings.

(a) An economic climate favourable to growth and a level of taxation which does not discourage saving.

(c) A social and political climate favourable to private individual and group action in providing for personal financial security.

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(b) An economic climate favourable to growth and a level of taxation which does not [illegible]

(c) A social and political climate favourable to private individual and group action in [illegible]oviding for personal financial security.

(d) A basic floor of security, as warranted by the nation's ability to provide it, for the aged, widows and orphans, the permanently disabled and the temporarily unemployed.

(e) Consistent protection of property rights under law to ensure stability and confidence in financial obligations.

(f) General freedom and flexibility in investment within a minimum of statutory limitations to make possible impelementation of long-term guarantees.

(g) Sound domestic environment within which all life insurance companies can operate for the benefit of Canadians and which will also facilitate effective operation of Canadian companies abroad. (Para. 7.44)

SECTION 3

DESCRIPTION OF THE INDUSTRY

STRUCTURE OF THE INDUSTRY

3.1 At the end of 1960 life insurance was provided in Canada by 99 companies registered under the federal insurance laws; by 22 Canadian companies operating under provincial charters without federal registry; and by a number of fraternal benefit societies. This submission relates only to the life insurance companies.

3.2 The federally-registered companies had in force in Canada $45 billion of life insurance or 95 per cent of that in force with all life insurance companies at the end of 1960. The provincial companies had $2 billion in force. Since 1935 the provincial companies have increased their share of the total from 1 per cent to 5 per cent (see Table 3.a).

Table 3.a

Life Insurance in Force in Canada *

	End of 1935		End of 1960	
	Amount (000,000)	% of Total	Amount (000,000)	% of Total
Federally-registered companies	$6,259	99	$44,649	95
Provincial companies	88	1	2,218	5
	$6,347	100	$46,867	100

* Fraternal benefit societies had $989 million of life insurance in force at the end of 1960.

3.3 At the end of 1960 the 99 federally-registered companies included 36 Canadian, 43 United States, 14 British, two German, two Swiss, one Australian and one

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Table 3.a

Life Insurance in Force in Canada *

	End of 1955 Amount (000,000)	End of 1955 % of Total	End of 1960 Amount (000,000)	End of 1960 % of Total
Federally registered companies	$6,259	99	$44,649	95
Provincial companies	83	1	2,218	5
	$6,347	100	$46,867	100

* Fraternal benefit societies had $939 million of life insurance in force at the end of 1960.

3.3 At the end of 1960 the 99 federally-registered companies included 36 Canadian, 43 United States, 14 British, two German, two Swiss, one Australian and one

of Netherlands origin. The number of companies has expanded significantly in the last 25 years. In 1935 there were 61 federally-registered companies. The origin of the companies and their respective shares of life insurance in force in Canada in 1935 and 1960 are shown in Table s.b.

Table 3.b

Life Insurance Companies in Canada
(Federally-Registered)

	End of 1935		End of 1960	
	Number of Companies	% of Life Insurance in Force	Number of Companies	% of Life Insurance in Force
Canadian	27	66.5	36	68.1
United States	20	31.5	43	28.2
British	13	1.5	14	3.5
Netherlands	-	-	1	.1
Swiss	-	-	2	.1
Australian	1	.5	1	-
German	-	-	2	-
	61	100.0	99	100.0

3.4 Fourteen of the Canadian companies do business outside of Canada. The $13 billion of life insurance they have in force abroad equals 42 per cent of their total business and 28 per cent of the total business of all Canadian companies. Seventy per cent of this business outside of Canada is on the lives of policy-holders in the United States, 16 per cent on persons in the British Isles, 2 per cent on Asians, 6 per cent on Africans, and 6 per cent on persons in the Caribbean area and Latin America.

3.5 Before World War II Canadian companies actively carried on business in some 64 different countries and territories. This number is now reduced to just over 30. During the War business was suspended in enemy and enemy-occupied countries and

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in some it has not been resumed. Since the War legislation governing the life insurance business in certain foreign countries has resulted in a withdrawal by the Canadian companies from those markets. Despite this, the business of the Canadian companies in force outside of Canada is still growing strongly - an acknowledgement of the reputation of these companies and their competitiveness in outside markets.

3.6 The life insurance companies had about 40,500 full-time personnel in their service in Canada at the end of 1960 - about 25,500 in administrative work and approximately 15,000 full-time field representatives. The operations of the Canadian companies outside Canada provided employment for more than 3,500 administrative and branch office personnel and 4,000 full-time field representatives in those countries where they are carrying on business. Of course, a large part of the supervisory and administrative work for these foreign branches is carried on in Canada. Many of the non-resident companies maintain Administrative offices in Canada for their Canadian business which employ Canadian personnel.

3.7 The comparable figures are not available for 1935 but in 1939, 19,700 Canadians were in the employ of the life insurance companies in Canada. During the last 20 years, personnel has doubled while the amount of life insurance in force increased seven-fold, annuities in force increased forty times, the annual amount of life insurance purchased rose ten-fold, annual benefits, including health insurance benefits, increased

in some it has not been resumed. Since the War legislation governing the life insurance business in certain foreign countries has resulted in a withdrawal by the Canadian companies from those markets. Despite this, the business of the Canadian companies in force outside of Canada is still growing strongly - an acknowledgement of the reputation of these companies and their competitiveness in outside markets.

3.6 The life insurance companies had about 40,500 full-time personnel in their service in Canada at the end of 1950 - about 25,500 in administrative work and approximately 15,000 full-time field representatives. The operations of the Canadian companies outside Canada provided employment for more than 3,500 administrative and branch office personnel and 4,000 full-time field representatives in those countries where they are carrying on business. Of course, a large part of the supervisory and administrative work for these foreign branches is carried on in Canada. Many of the non-resident companies maintain Administrative offices in Canada for their Canadian business [illegible]

3.7 The comparable figures are not available for 1925 but in 1939, 19,700 Canadians were in the employ of the life insurance companies in Canada. During the last 20 years, personnel has doubled while the amount of life insurance in force increased seven-fold, annuities in force increased forty times, the annual amount of life insurance purchased rose ten-fold, annual benefits, including health insurance benefits, increased

four times and assets increased $3\frac{3}{4}$ times.

OWNERSHIP OF THE LIFE INSURANCE COMPANIES

3.8 Table 3.c shows the number of Canadian life insurance companies doing business in Canada at the end of 1960 that were mutual companies - that is, companies owned and controlled by policyholders - and the number that were companies with capital stock held by shareholders.

Table 3.c

Mutual and Stock Life Insurance Companies in Canada

End of 1960

	Mutual	Stock	Total
Canadian companies			
Federally-registered	9	27 *	36
Provincial	11	11	22
Non-resident companies	21	42	63

* Five of these were in the process of becoming mutual.

3.9 Federal law requires that at least one-third of the directors of a Canadian stock company issuing participating policies must be elected by the holders of the company's participating policies and no shareholder is eligible to be a policyholders' director. Also, the law effectively limits dividends to shareholders by stipulating the proportion of "profits" on participating insurance * that must be retained for participating policyholders. These proportions are on a graded scale; policyholders must be credited with at

* Participating insurance represents more than 60 per cent of the life insurance in force in Canada with stock companies.

least 90 per cent of such profits in small companies and at least $97\frac{1}{2}$ per cent in large companies.

3.10 The controlling interest in twelve of the 38 Canadian stock life insurance companies today lies outside Canada (two in Great Britain, five in Continental Europe and five in the United States). These twelve companies had 6 per cent of the life insurance in force with all Canadian companies as at the end of 1960. Four of these companies were formed substantially on the basis of foreign capital. In the case of the remaining eight companies, control of one passed out of Canada in 1929 while control of the remaining seven passed out of Canada since 1954.

3.11 The Canadian and British Insurance Companies Act prohibits a company from investing its life insurance funds in the shares of another life insurance company. This prohibition has reduced the number of potential Canadian purchasers of the controlling interest in life insurance companies where it is "up for sale" and may have militated against the retention of ownership of Canadian companies in Canada.

3.12 In 1957, however, in order to help overcome this problem, federal legislation was enacted to permit Canadian stock companies to mutualize, that is, to acquire their own shares. Five companies have now done this or are in the process of doing so. At the end of 1960, 59 per cent of the life insurance in force with Canadian companies was with mutual companies or companies that shortly will be mutual.

3.13 Twenty-five Canadian companies have entered

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3.13 Twenty-five Canadian companies have entered

the life insurance field between 1935 and 1960. Because of the particular importance of adequate financing for the protection of policyholders in the early years of a new life insurance company, fifteen of these have been stock companies and of the ten mutual companies all were either reorganized fraternal benefit societies or affiliates of non-life insurance or other financial institutions.

3.14 Recently a Canadian stock company took over the business of a Canadian mutual company with the approval of the latter's policyholders and the Treasury Board. This is the first merger involving Canadian companies since 1935. In view of the influx of new companies and the mutualization of some stock companies it may be said that on the whole there has been a marked trend toward wider dispersion of the overall ownership of the life insurance industry.

BUSINESS IN FORCE

Life Insurance

3.15 At the end of 1960 Canadians owned $47 billion of life insurance, almost eight times the 1935 amount. Between 1935 and the outbreak of World War II, life insurance grew slowly. Since then the total has increased an average of 11 per cent per year. The growth of life insurance in force is set out in Table 3.d.

Table 3.d

Life Insurance in Force in Canada

End of Year	Amount in Force (000,000)	Individual Amount (000,000)	Individual % of Total	Group Amount (000,000)	Group % of Total
1935	$ 6,347	$ 5,836	92	$ 511	8
1940	7,041	6,310	90	731	10
1945	9,964	8,894	89	1,070	11
1950	16,229	13,614	84	2,615	16
1955	26,624	20,271	76	6,353	24
1960	46,867	32,128	68	14,739	32

3.16 A factor in this growth has been group insurance. As Table 3.d indicates, life insurance transacted on a group basis represented 32% of the total in force at the end of 1960 while that acquired on an individual basis equalled 68%. In 1935 group insurance represented 8%. In 1960, 86% of those employed in Canadian industry were in firms with a group insurance plan.

3.17 In recent years some organizations in the savings and consumer credit field have added a life insurance feature to the financial arrangements offered their customers. At the end of 1960, 19% of the group insurance in force covered individuals who had entered into such special credit or savings plans.

3.18 About three out of every four Canadian families own life insurance. The average amount owned per household at the end of 1960 was about $10,400. The average varied from $6,400 in the Atlantic Provinces to $12,400 in Ontario.

3.19 A principal function of life insurance is to protect families against the cessation of earnings at the death of the head of the family. An important test of the adequacy of life insurance protection is to relate the amount of such protection to earned income - on an individual or national basis.

3.20 In 1960 Canadians held life insurance in an amount 2.2 times their total wages, salaries and the earnings of the self-employed. The corresponding ratio in the United States was just over 1.7 times.* Table 3.e illustrates the trend in the Canadian ratio since 1920.

Table 3.e

Ratio of Life Insurance to Earnings in Canada

Year	Life Insurance in Force - End of Year (000,000)	Ratio to Wages, Salaries and Self-Employed Income during Year
1920	$ 2,675	1.0 (est.)
1925	4,212	1.4 (est.)
1930	6,588	1.8
1935	6,347	2.4
1940	7,041	1.8
1945	9,964	1.3
1950	16,229	1.4
1955	26,624	1.6
1960	46,867	2.2

3.21 As indicated in Table 3.f, in 1960 the ratio of life insurance owned to total earned income in the ten provinces ranged from 1.1 to 1 in Newfoundland to 2.5 to 1 in Quebec. However, seven of the provinces were within a narrow range, indicating a fairly close relationship between life insurance in force and earned income.

Table 3.f

Ratio of Life Insurance to Earnings by Province - 1960

Province	Life Insurance in Force - End of Year (000,000)	Ratio to Wages, Salaries and Self-Employed Income during Year
Newfoundland	$ 342	1.1
Prince Edward Island	126	1.8
Nova Scotia	1,330	2.1
New Brunswick	918	2.0
Quebec	13,534	2.5
Ontario	19,913	2.2
Manitoba	1,995	1.8
Saskatchewan	1,442	1.4
Alberta	2,978	1.8
British Columbia	3,920	1.7

3.22 Annuities

There were 649,000 annuity contracts or certificates in force with life insurance companies in Canada at the end of 1960. These provide

* This ratio is based on private life insurance and therefore excludes the survivorship benefits provided under the public Old-Age, Survivors, and Disability Insurance program.

for present and future annual payments to annuitants of $736 million per year. In 1935 there were 46,000 contracts in force with annual payments of $18 million. Growth in the intervening years is outlined in Table 3.g.

Table 3.g

Annuities in Force in Canada

(Federally-Registered Companies)

End of Year	Annual Payment (000,000)	Individual	Group	Settlement and Disability
1935	$ 18	49%	29%	22%
1940	50	40	49	11
1945	79	35	55	10
1950	203	20	75	5
1955	382	13	83	4
1960	736	8	90	2

3.23 Group annuities represented 29 per cent of the 1935 total of all annuities in force compared with 90 per cent of the 1960 total. The growth of new group contracts in force has been an even more important factor in the annuity area than in the life insurance field.

3.24 Sixty-nine per cent of the annuities now in force are with Canadian companies and 31 per cent with United States and British companies.

3.25 The relative importance of annuities in the life insurance companies' rule as gatherers of savings is indicated by the fact that 26 per cent of the companies' reserve liabilities in Canada at the end of 1960 related to annuities - 5 per cent to individual annuities, 19 per cent to group annuities and 2 per cent to annuities arising out of the settlement and disability provisions of the companies' contracts.

3.26 In 1960 the life insurance companies were

administering about $1.2 billion of assets relating particularly to the provision of group pensions. In comparison, the group pension plan reserves of the federal government's Annuities Branch equalled $600 million and the assets of trusteed pension plans totalled $3.6 billion.

Health Insurance

3.27 In addition to their life insurance and annuity services, over 30 life insurance companies are providing more than 5 million Canadians with insurance covering medical and surgical expenses,over 4 million with insurance for hospital expenses not covered by government hospitalization plans, and over 1.3 million workers with loss of time (weekly indemnity) insurance.

3.28 Health insurance is also provided by casualty insurance companies, medical care plans sponsored by the medical profession, and by Blue Cross and other voluntary plans.

PREMIUM INCOME

3.29 Premium income in Canada during 1960 totalled $1.1 billion. Life insurance premiums accounted for $769 million, annuity considerations $184 million and health insurance premiums $129 million.

3.30 Throughout the 1930's, payments for life insurance and annuities were maintained at a remarkably steady level despite economic difficulties. In part this can be attributed to the use by many policyholders of the loan provisions in their contracts for the payment of premiums. Since 1940 premium payments have risen each year in absolute amount. This along with the

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[illegible]

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ratio to disposable income is set forth in Table 3.h.

Table 3.h

Ratio of Premiums* to Disposable Income ** in Canada

Year	Premiums*	% of Disposable Income **
1930	$ 226	5.3
1935	211	6.5
1940	217	4.5
1945	296	3.6
1950	443	3.5
1955	650	3.6
1960	953	3.8

*Includes annuity considerations but not health insurance premiums.

**Personal income less personal direct taxes.

BENEFIT PAYMENTS

3.31 As the ownership of life insurance and annuities has increased and the policies in force have aged, payments to policyholders and beneficiaries have grown materially. In 1960 life insurance and annuity benefits paid by all life companies amounted to $560 million, compared with just over $160 million in 1935 and 1945.

3.32 Table 3.i gives an analysis of the benefit payments made by federally-registered companies. Death claims since 1945 have accounted for less than 40 per cent of total payments. The balance in the main represents payments to living policyholders. The reliance placed by policyholders on the cash surrender provisions during the economic difficulties of the 1930's is illustrated in the 1935 figures.

ratio to disposable income is set forth in Table 3.h.

Table 3.h

(Ratio of Premiums* to Disposable Income ** (in millions)

Year	Premiums*	% of Disposable Income **
1930	$ 226	5.3
1935	211	6.5
1940	217	4.5
[illegible]	[illegible]	[illegible]
1950	443	3.5
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Table 3.i

Benefit Payments in Canada

(000,000 omitted)

Year	Death Claims	Matured Endowments	Disability Claims	Cash Values	Policy Dividends	Annuity Payments	Total
1935	$ 42	$ 13	$ 3	$ 71	$ 30	$ 3	$162
1940	50	24	3	54	30	7	168
1945	68	28	3	26	29	10	164
1950	86	35	4	53	41	20	239
1955	124	34	4	71	69	35	337
1960	196	46	5	129	109	75	560

LEVEL-PREMIUM LIFE INSURANCE

3.33 The regular methodical purchase of level-premium plans of life insurance by millions of Canadians is the basis for the accumulation of funds in the companies.

3.34 Under level-premium plans the amount of the annual premium remains unchanged throughout the premium-paying period although the probability of death of the insured person increases as time goes on. In the early years of a level-premium policy, the likelihood of death is low in relation to later years and the premiums paid for a block of like policies exceed death claims. In the later years of the block of policies, the premiums paid are less than the amounts necessary to meet the claims that come with advancing years and rising mortality or the maturity of the policy.

3.35 When a level-premium plan is issued, a fund or reserve must be accumulated in the early years to meet the rising level of claims that will occur during the later years of such policies. These reserve requirements lead to the accumulation of personal saving through life insurance.

3.36 The extent to which reserves are built up varies with the type of level-premium plan. Term life insurance covers the possibility of

death during the limited term of the polich while a straight life policy is based on the certainty of the death of the insured and the certainty that the death benefit must be paid. A five-year or longer term policy would be written on a level-premium plan but the short duration and the very nature of such a policy would not require a reserve accumulation during the five years or other term of nearly the size that would be necessary under a straight life policy that would be expected to carry on many years until the death of the insured. In turn, the rate of reserve accumulation under an endowment policy is greater than under straight life or other so-called life policies since the payment of the endowment benefit is due either at the end of a specific period of, say, 20 years or at the death of the insured if earlier.

3.37 There are, of course, other factors affecting the rate of accumulation of funds inthe companies, for example, the rate of investment earnings, the extent of cash withdrawals in the case of policies having reserves and the degree to which beneficiaries leave policy proceeds (including policyholder dividends) on deposit with the company to earn interest.

RECENT TRENDS IN NEW BUSINESS

3.38 Purchases of life insurance in Canada amounted to $6.1 billion during 1960, ten times the 1935 figure. This is set forth in Table 3.j.

Table 3.j

Life Insurance Purchased in Canada

Year	Purchases (000,000)	Individual* Amount (000,000)	%	Group* Amount (000,000)	%
1935	$ 602	$ 582		$ 20	3
1940	604	575		29	5
1945	1,057	991		66	6
1950	1,900	1,642		258	14
1955	3,454	2,763		691	20
1960	6,129	4,576		1,553	25

*Figures for the provincial companies are estimated for earlier years. Comparison with Table 3.d shows that group insurance represents a smaller proportion of purchases than of business in force. The main reason for this is that normal increases in insurance under an existing group contract are not considered to be purchases of new insurance.

3.39 A substantial part of the 1960 purchases was temporary or term insurance and that portion has been increasing in recent years. For example group insurance, which is almost always term insurance, accounted for 25 per cent of 1960 purchases. In 1935 group insurance represented only 3 per cent of new purchases. With respect to life insurance purchased by individuals, 42 per cent was on a term basis in 1960 compared with 8 per cent in 1935. Much of this term insurance takes the form of family income, mortgage redemption and other special policies which combine term with permanent forms of insurance. The increase in term insurance reflects a growing public recognition of the need for substantial amounts of protection.

3.40 As a result, purchases of the "permanent" life

insurance plans, that is, those which contain a savings element, have declined as a proportion of the total. Nonetheless, purchases of such plans have increased in absolute terms. In 1935 purchases of "permanent" plans amounted to $400 million, in 1945 $600 million and in 1960 $2.6 billion. This is exclusive of the increasing proportion of saving which has been done in the form of annuities.

ASSETS

3.41 The assets relating to the life insurance and annuity business in Canada totalled $8,260 million at the end of 1960. Of this, 70 per cent was held by Canadian federally-registered companies, 3 per cent by provincial companies and 27 per cent by United States, British and other European companies to cover their Canadian liabilities. In addition, assets relating to the life companies' health insurance operations in Canada amounted to about $80 million.

Table 3.k

Life Insurance Assets Held in Canada

(000,000 omitted)

End of Year	Federally-Registered Companies	Provincial Companies	Total
1935	$ 1,828	$ 40	$1,868
1940	2,220	46	2,266
1945	2,886	52	2,938
1950	3,997	79	4,076
1955	5,599	125	5,724
1960	8,007	253	8,260

3.42 At the end of 1960 the assets held outside of Canada by Canadian companies on behalf of and for the protection of policyholders and annuitants abroad amounted

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3.42 At the end of 1960 the assets held outside of Canada by Canadian companies [illegible] policyholders and annuitants abroad amounted

to $2,860 million. At the same time assets held in Canada by non-resident companies for the protection of Canadian policyholders amounted to $2,260 million.

3.43 Detailed analysis of the composition and growth of the life insurance companies' assets in Canada and their importance in the economy is provided in sections 4 and 5 of this submission.

SUPERVISION OF INSURANCE

3.44 The federal and provincial governments in Canada have shared responsibility for the supervision of the insurance business in Canada since 1868 when the first federal Insurance Act was passed. For many years before that time insurance legislation had existed in some provinces. Since that time, provincial laws have developed alongside of federal laws and insurers have been incorporated under both federal and provincial laws.

3.45 Briefly, the federal department of Insurance concerns itself with the solvency of insurers and the provincial Departments mainly with the regulation of the business. The practical division of responsibility may be summarized as follows:

(a) The federal Department registers all federally-incorporated Canadian insurers, all non-Canadian insurers doing business in Canada and, in addition, a few provincial companies that have voluntarily placed themselves under its jurisdiction. It inspects insurers registered by it and administers legislation respecting the valuation of assets and liabilities, deposits, solvency, etc., of

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these insurers.

(b) Whether or not they hold federal certificates of registry all insurers must be licensed in each province (except Nova Scotia) in which they operate. Three provinces - Manitoba, Newfoundland and Nova Scotia - will not permit insurers to transact life insurance within their jurisdictions unless they are registered at Ottawa. The provinces require documents of incorporation, etc., to be filed initially by each insurer and thereafter annual statements showing its general financial condition and particulars of its business in the province. The provinces do not inspect or require deposits from federally-registered insurers.

(c) The provincial Departments supervise and assume responsibility for inspections relating to the solvency of insurers not registered with the federal Department.

(d) The provinces exclusively legislate respecting:

(i) insurance contracts and the terms, conditions and incidents thereof; and

(ii) the licensing and regulation of agents, brokers and adjusters,

and enforce this legislation.

3.46 While many of the provisions of the first federal Insurance Act of 1868 are traceable in the insurance legislation of the present day, probably the most important single federal enactment respecting insurance since Confederation was the Insurance Act of 1910. Except for the imposition of a limit on common

[illegible] insurers.

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and enforce this legislation.

3.46 While many of the provisions of the first federal Insurance Act of 1868 are traceable in the insurance legislation of the present day, probably the most important single federal enactment respecting insurance since Confederation was the Insurance Act of 1910. Except for the imposition of a limit on common

stock investment in 1932 and the introduction of the so-called "basket" clause in 1948, the investment powers of the companies as detailed in the Act of 1910 stood without substantial change until 1950. In that year and again in 1961 they were further enlarged in important particulars. The current investment powers are reviewed in section 4.

3.47 By and large, insurance legislation and government regulation have been well conceived and administered in Canada for more than one hundred years and are entitled to a share of the credit for the unique record represented by the fact that no policyholder in a Canadian legal reserve life insurance company has ever lost a dollar through non-payment of the amount guaranteed under his policy at death or on maturity. Canadians insured with companies from other countries doing business in Canada have, for more than 75 years, been equally well served. As new forms of investment, new forms of cover and new problems have developed, amendments to the legislation have been made.

3.48 The division of authority between the federal and provincial governments in the matter of the supervision of insurance, and particularly a suggestion that the supervision and regulation of the business should be undertaken exclusively by the federal government, were considered by the Royal Commission on Dominion-Provincial Relations in January, 1938. The views of the Association were placed before that body in the form of the following resolution.

"The Canadian Life Insurance Officers

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"The Canadian Life Insurance Officers

> Association suggests that the law of life insurance contracts, as exemplified by the Uniform Life Insurance Act of the Canadian Provinces and comparable provisions in the Quebec Civil Code, and the licensing of life insurance agents, be within exclusive provincial jurisdiction, but that all other matters concerning the supervision (licensing, solvency, investments, inspections and reports) of life insurance companies doing business in more than one province, and the regulation of life insurance business generally, be within the exclusive jurisdiction of the Dominion."

The Association went on to say that it felt that the foregoing resolution recognized the national character of the life insurance business in its proper relation to local interests and existing political and other conditions in Canada and hoped that the Commission would recommend that the British North America Act, 1867, be amended to give effect to the substance of the resolution and to make certain that the respective powers of the federal government and the provinces with respect to life insurance are clearly defined. The Commission generally endorsed the Association's stand but the suggested change in the constitution has not been made.

LIVE INSURANCE REPORTS

3.49 The federally-registered life insurance companies make exhaustive reports to the Superintendent of Insurance on forms prescribed by him. These reports

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The federally registered life insurers make extensive reports to the Superintendent [illegible]

set forth all aspects of a company's business in great detail. The results are summarized each year in the Report of the Superintendent of Insurance for Canada. That part related to life insurance runs to some 900 pages. The life insurance companies engaged in the health insurance business report separately on this branch of their business. Provincial companies make similarly detailed reports to their Superintendents. The reports of the Superintendents are readily available but to the uninitiated they may represent a very formidable array of figures.

3.50 Companies, of course, present statements of their affairs at their annual meetings. In the case of a Canadian federally-registered company, notice of such meeting must be given at least 15 days before in two or more daily newspapers in or near the head office city and premium notices or receipts at least once each year must contain a statement of the participating policy-holder's right to attend and vote in person or by proxy at such meeting.

3.51 The life insurance business is a complicated one involving as it does so many forward judgments relative to the mortality, expense and interest factors. Comparison as between companies requires exhaustive and competent analysis which unfortunately is beyond the capacity of most laymen. No satisfactory method has yet been found to produce a simple index or indices for comparative purposes.

3.52 Comparison of the "net earned interest rate" which is published affords someindication of the results

accruing from a company's investment operation but can only be used with some qualification. It may be affected by a company's treatment of asset values and investment expense apportionment. Further the published rate is based on the company's total assets. Where a company has assets outside of Canada, the rate is of course influenced by the yields obtained abroad. If a "net earned interest rate" on Canadian assets alone were thought to be desirable, the companies could undoubtedly develop it.

3.53 Despite the detailed information available, the difficulty of making valid comparisons between companies in the fields of expense and mortality seems to be even greater. Expenses tend to vary directly with the degree of service rendered while mortality tends to reflect the experience of the population groups insured. Certainly no all-inclusive method could yield unqualified measures of either of these diverse elements.

3.54 Comparison of premium levels, dividends and cash surrender values for strictly comparable policies in different companies affords the buyer possibly the easiest and best comparison. Such information is available in handbooks published by an independent agency. Even this extensive information can only be used with some qualification. It is difficult to find "strictly comparable" policies and any comparison is likely to fail to take into account important policy provisions. It will also fail to take into account the service that may be expected both from the company and from the agent and the company's policy with regard to dividend

distribution. The most important considerations to most prospective purchasers are likely to be beyond the scope of mechanistic comparison.

COMPETITION

3.55 There is intense competition among life insurance companies in the life insurance, annuity and health insurance fields. This competition within the industry shows no signs of decreasing. Since 1935 for example, the number of federally-registered life insurance companies in Canada increased 50 per cent. Despite the more rapid growth in the number of non-resident life companies operating in Canada, the Canadian life companies have increased their proportion of life insurance in force (see Table 3.b.).

3.56 Competition within the industry is further indicated by the decline in the share of life insurance in force held by the larger companies. For example, in 1935 the five largest companies held 53 per cent of the business in force; in 1960 these same companies held 48 per cent. The next five companies had on their books 24 per cent of the total life insurance in force in 1935; in 1960 these same five companies held 19 per cent of the total. In 1935 the largest share held by any one company was 16½ per cent; in 1960 the largest company, which had been third largest in 1935, had 12 per cent.

3.57 The benefits of competition accrue to policyholders and annuitants. For example, since 1950 one medium-sized company has reduced its whole life non-participating rates eight times, increased its dividend scale five times

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3.57 The benefits of competition accrue to policy-holders and annuitants. For example, since 1950 one medium sized company has reduced its whole life non-participating rates eight times, increased its dividend scale five times

and changed its group pension rates fifteen times to keep the price of its products in line with changing interest, mortality and expense experience, and abreast of competition. Other companies have likewise made frequent adjustments. Competition has led to the widespread adoption of such recent innovations as the graduation of premiums by size of policy, the family plan, special rates for women and guaranteed insurability. In the group field where policies are subject to annual renewal and review, competition centers on fractional differences in price arising from the inevitable variations in the evaluation of the risk among the quoting companies. In the pension field an individual company may offer the choice of group annuity, deposit administration or variable accumulation approaches to funding. The widespread introduction of computers will undoubtedly lead to further flexibility in the fashioning of contracts in all fields with a consequent increase in competition in this respect.

3.58 Investment earnings are a vital factor in the determination of the cost of insurance to policyholders. Competition among individual companies in the investment aspects of the business is discussed in section 5. Aspects of the industry's competition with other savings institutions are discussed in section 7.

3.59 Life insurance has always had to be sold. Most people require some persuasion to put aside for tomorrow a dollar which is available to be spent today. This is the continuing task of life insurance representatives. Also, in the fact of the complexities of law,

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taxation and estate administration, the tailoring of life insurance programs to changing needs requires continuing service as well. Qualified field representatives who do this selling and servicing have been responsible in large measure for the growth in insurance protection and for the pre-eminent position the life insurance industry enjoys as a collector of voluntary personal savings.

SECTION 4

THE POSITION OF THE LIFE INSURANCE INDUSTRY IN THE CANADIAN FINANCIAL SYSTEM

4.1 In consequence of their primary function of providing life insurance and annuities, the life insurance companies have been important financial intermediaries within the Canadian financial system for more than 100 years.

LIFE INSURANCE SAVING

4.2 A significant portion of Canadian saving is channelled through the life insurance companies. Hence, the industry occupies a very important position in the structure of our capital market as a supplier of new investment funds. These savings dollars arise from two principal sources - premiums for insurance and annuities and investment income. Over long periods of time life insurance saving has tended to vary with personal income. Maintenance of this relationship, of course, will depend upon the relative relative attractiveness of this form of saving for the individual as well as the prevalence of a reasonably stable economic and financial environment.

4.3 The relative importance of life insurance saving in Canada is set forth in Table 4.a which displays the relationship between estimated insurance saving and both disposable personal income and personal saving for the period 1926-60.

4.4 The derivation of estimated life insurance saving for the period 1950-60 is shown in Table 4.b. Premium income is the largest single component of total

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income although it has dropped from 78 per cent to 72 per cent during the period. This reflects the trend toward a greater proportionate sale of temporary or term coverage and the increase in the rate of investment earnings.

4.5 Certain relationships are clear. In periods relatively free of extraordinary economic and financial events (such as depression, war or rapid inflation) annual changes in insurance saving tend to move fairly closely with movements in disposable personal income. A prolonged economic decline tends to have a relatively heavier impact on this form of saving than it does on income while on the other hand, in periods of rapid inflation, with income rising, the increase in insurance saving tends to respond more slowly.

4.6 The period since 1952 has been relatively free of the extreme economic and financial developments that characterized the preceding 23 years. Disposable personal income displayed a relatively steady growth and as the period advanced there was an important slowing down in the rate of price inflation. Under such conditions life insurance saving appears to bear a fairly consistent relationship to disposable personal income - a relationship of the order of 1.75 per cent. In 1960 this represented $450 million.

4.7 The relationship between life insurance saving and personal saving, so defined in the National Accounts, is difficult to measure satisfactorily. The personal saving series in the National Accounts is the residual compenent of the calculation and as such may not be too

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Table 4.a

Life Insurance Saving, Disposable Personal Income and Personal Saving

1926 - 1960

Year	A. Life Insurance Saving* (000,000)	B. Disposable Personal Income (000,000)	A/B	C. Personal Saving (000,000)	A/C
1926	$ 77	$ 3,961	1.94 %	$ 419	18.4 %
1927	83	4,175	1.99	282	29.4
1928	95	4,495	2.11	181	52.5
1929	81	4,540	1.78	- 81	-
1930	74	4,267	1.73	- 100	-
1931	63	3,552	1.77	- 221	-
1932	29	2,951	0.98	- 243	-
1933	46	2,721	1.69	- 263	-
1934	73	3,070	2.38	- 112	-
1935	80	3,268	2.45	- 70	-
1936	89	3,452	2.58	- 97	-
1937	87	3,895	2.23	11	790.0
1938	86	3,953	2.18	56	153.6
1939	81	4,178	1.94	194	41.8
1940	84	4,775	1.76	287	29.3
1941	108	5,555	1.94	452	23.9
1942	125	6,898	1.81	1,398	8.9
1943	159	7,344	2.17	1,536	10.4
1944	172	8,027	2.14	1,753	9.8
1945	178	8,311	2.14	1,342	13.3
1946	184	8,923	2.06	892	20.6
1947	183	9,584	1.91	494	37.0
1948	192	11,079	1.73	994	19.3
1949	208	11,849	1.76	926	22.5
1950	209	12,688	1.65	662	31.6
1951	228	14,794	1.54	1,334	17.1
1952	245	16,072	1.52	1,291	19.0
1953	279	16,904	1.65	1,312	21.3
1954	307	16,984	1.81	809	37.9
1955	342	18,239	1.88	850	40.2
1956	343	20,153	1.70	1,320	26.0
1957	344	21,274	1.62	1,202	28.6
1958	407	22,914	1.78	1,674	24.3
1959	444	24,236	1.83	1,754	25.3
1960	450	25,084	1.79	1,675	26.9

Sources: Dominion Bureau of Statistics and C.L.I.O.A.

*Methods used to estimate life insurance saving are outlined in Appendix 3.

Table 4.b

Some Components of Life Insurance Saving in Canada 1950 - 1960

(000,000 omitted)

Year	Premium Income (incl. that for settlement annuities)	Net Deposits Left with Companies At Interest	Investment Income*	Total Income	Total Outgo	Net Income	Increase in Policy Loans	Net Life Insur. Saving	Insurance Saving as % of D.P.I.	Insurance Saving as % of Personal Saving
1950	$453.5	$ 9.7	$130.1	$593.3	$372.4	$220.9	$11.7	$209.2	1.65	31.6
1951	501.7	4.2	143.7	649.6	401.5	248.1	20.6	227.5	1.54	17.1
1952	522.6	.8	156.3	679.7	421.0	258.7	14.0	244.7	1.52	19.0
1953	565.4	.3	180.5	746.2	455.1	291.1	12.2	278.9	1.65	21.3
1954	616.7	4.3	203.3	824.3	501.7	322.6	15.3	307.3	1.81	37.9
1955	666.0	7.8	232.2	905.8	552.7	353.1	10.6	342.5	1.88	40.2
1956	726.5	5.5	263.2	985.2	620.9	364.3	21.5	342.8	1.70	26.0
1957	790.4	-2.4	286.4	1,074.4	704.3	370.1	25.8	344.3	1.62	28.6
1958	861.5	8.2	303.7	1,173.4	754.3	419.1	12.0	407.1	1.78	24.3
1959	941.6	3.2	330.9	1,275.7	812.7	463.0	19.0	444.0	1.83	25.3
1960	967.0	8.2	372.0	1,347.2	874.3	472.9	23.0	449.9	1.79	26.9

Source: C.L.I.O.A. - See Appendix 3 for an outline of the methods of estimation used.

* Interest, dividends and rents adjusted for capital gains and losses without deduction of investment expenses.

precise. Despite this limitation, however, it is clear that life insurance saving does represent a very significant proportion of total personal saving during the war years, when personal saving rose substantially and the percentage relationship of life insurance saving declined to around 9 per cent. On the other hand, during the depression there was net personal dissaving in Canada and yet life insurance saving remained positive.

4.8 The period 1956-60 seems to show a relatively stable relationship between the two measures of saving. During this time, life insurance saving appears to account for approximately 26 per cent of total personal saving in Canada.

INVESTMENT REGULATION

4.9 The investment operations of federally-registered life insurance companies in Canada must conform to the provisions of the Canadian and British Insurance Companies Act and the Foreign Insurance Companies Act. These define certain broad categories of investments in which life insurance funds may be placed, and impose certain additional limitations within some categories. They also define certain investments which are prohibited.

4.10 Broadly speaking, the chief categories in which life insurance funds may be invested are as follows:

(a) Bonds, direct and guaranteed, of the governments of Canada and other Commonwealth countries, the United States of America and other countries or subdivisions in which the company does business.

[illegible]
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(a) Bonds, direct and guaranteed, of the governments of Canada and other Commonwealth countries, the United States of America and other countries in [illegible]

(b) Bonds, direct and guaranteed, of a municipality in Canada or any other country in which the company is carrying on business.

(c) Corporation bonds fully secured by mortgage on property.

(d) Equipment trust certificates issued for the purchase of transportation equipment for use on railways or public highways by a Canadian or United States corporation.

(e) Corporation debentures, provided the corporation has consistently paid dividends on its shares for at least the preceding five years or has had satisfactory earnings in that period.

(f) Guaranteed investment certificates issued by a Canadian trust corporation, provided the corporation has consistently paid dividends on its shares for at least the preceding five years.

(g) Preferred shares, provided the corporation has paid dividends on such shares or on its common shares (of at least 4 per cent of stated value) for at least the preceding five years.

(h) Common shares, provided the corporation has paid dividends of at least 4 per cent of the stated value of the shares for the preceding seven years.

(i) Mortgage loans on real estate not to exceed 66-2/3 per cent of the value of such real estate, or loans in excess of this limit if the excess is guaranteed or insured by a government, and mortgage loans under the National Housing Act.

(j) Real estate or leaseholds for the production

of income, providing the leasing corporation has a dividend record that would qualify its debentures (see item (e) above) and the lease requires repayment of at least 85 per cent of the amount invested within the period of the lease; in any case, this amount should be repaid in not more than thirty years.

(k) Real estate for its own use. Real estate acquired through foreclosure of mortgage loans does not qualify as an asset after a limited period of years.

(l) Ground rents.

(m) Construction and operation of low-cost or moderate-cost rental housing projects and the purchase and improvement of land for housing development, in accordance with the National Housing Act. The aggregate so invested may not exceed 5 per cent of the company's total assets in Canada.

(n) Loans to policyholders on the security of the company's policies.

(o) Other investments not specifically authorized by the Acts, in an aggregate amount not exceeding 5 per cent of the company's total assets.

The Acts also provide that:

(p) No investment may be made in any security on which payment of principal or interest is in default.

(q) No insurance company may invest its life insurance funds in the shares of any other company transacting the business of life insurance.

(r) No insurance company may invest in more than 30 per cent of the shares of any one corporation, nor may it invest more than 15 per cent of its assets in common

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(r) No insurance company may invest in more than 30 per cent of the shares of any one corporation, nor may it invest more than 15 per cent of its assets in com-

shares.

(s) A company may not invest more than 10 per cent of its assets in income-producing real estate.

(t) No insurance company may make a loan to any of its directors or officers or to the wife or child of any such director or officer, except on the security of their own life insurance policies.

(u) No insurance company may lend to any corporation if more than one-half of the shares of the capital stock of that corporation are owned by any director or officer of such insurance company or the wife or child of any such director or officer or by any combination of such persons.

4.11 The provincial insurance laws also contain provisions governing investment of life insurance funds held by provincial companies.

4.12 The investments in Canada of a non-resident company that are deposited or vested in trust under one of the Insurance Acts (and these must at least equal the company's liabilities in Canada) are subject to the restrictions of those Acts. Investments not held in trust are subject only to any applicable restrictions in the laws of the country of origin of the non-resident company.

4.13 The so-called "basket" clause referred to in item (o) above permits investment in assets that do not meet the specific eligibility tests. Some may be new types of investment that may in time be specifically recognized. Some will qualify in due course under the existing provisions as, for instance, they acquire an earnings or dividend record. The clause does not, however,

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permit investment in mortgage loans in excess of 66-2/3 per cent of the value of the property (item (i) above) nor does it ease any of the restrictions in items (p) to (u).

4.14 Within this framework there exists ample room for a significant variation in the conduct of investment operations by the individual companies as they attempt to achieve their investment objectives on behalf of their policyholders. From the viewpoint of the economy participation is possible in almost every important area without severe limitation.

Legislative Changes in 1961

4.15 The investment provisions of the Insurance Acts are kept under constant review by the life insurance companies and by the supervisory authorities and as the need arises amendments are proposed thereto. The investment provisions in the federal Acts were revised substantially both in 1950 and in 1961. The provincial statutes have been amended from time to time to reflect changing conditions.

4.16 The major changes made in the investment provisions of the federal law in 1961 were the increase in the valuation limit on mortgages from 60 per cent to 66-2/3 per cent, the increase from 3 per cent to 5 per cent on non-specified investments, and the increase from 5 per cent to 10 per cent on income-producing real estate.

4.17 The amendments also provided that a segregated fund must be maintained for policies the reserves for which "vary in amount depending upon the market value

of a specified group of assets", namely, variable accumulation funds or variable annuities. Where such a fund is maintained, the 15 per cent limit on common share investments and the 10 per cent limit on income-producing real estate do not apply to the investments constituting the assets of the fund. However, the 5 per cent limit for non-specified investments does apply to each segregated fund.

4.18 During the discussions with the regulatory authorities prior to the amendments, the life insurance companies had also asked for relaxation of both the 15 per cent limit on common stocks relating to their regular lines of business and the provisions governing the valuation of assets. On the first point, the Association submitted the following to the Superintendent of Insurance in 1959:

> "Although the Canadian companies presently hold much less than 15 per cent of their assets in common shares there is a strong feeling, both within the companies and elsewhere, (e.g., the Report of the Royal Commission on Canada's Economic Prospects), that under appropriate market conditions the present limit might be too restrictive. Also, some of the non-resident companies are now finding the limit restrictive.
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> "Common share investments offer the companies an opportunity to participate in the growth of industrial and commercial corporations. Naturally, the returns on such investments must be attractive and at the moment other

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forms of investment are, generally speaking, relatively more attractive for life insurance companies. However, the companies desire to be in a position to take greater advantage than the 15 per cent limit would permit of such market opportunities as the future may present. The companies therefore propose that the limit be raised to 25 per cent."

4.19 On the matter of valuation, the existing law provides that the Canadian life insurance companies must value bonds, debentures and stocks at market values at year-end, except for redeemable securities not in default issued or guaranteed by Canada or any province, the United Kingdom or the United States, which are to be taken at amortized values. (The amortized value exception was added to the law in 1950). The value of all securities in the annual statement must not exceed in total this combination of market and amortized values. In view of the fact that the obligations of the life insurance company do not fall due at any one time and are of a long-term character, the majority of the companies believed that futther relief from the constraints of year-end market valuation was desirable. They pointed out that a sharp shift in the market can result in substantial temporary encroachments on surplus funds. This tends to produce inequities as well as leading to unwarranted conclusions regarding surplus depletion in the incidence of distribution of surplus to policyholders.

4.20 The Association's 1959 submission on this point, based on the majority view, proposed two changes

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in the valuation standard: that (a) municipal securities of Canada, the United Kingdom and the United States of America and (b) securities of states of the United States should be added to the list of those securities for which amortized values are to be used, and that for all other securities and shares the average of the three most recent year-end market values should be used. It was suggested that the use of amortized values for municipal securities would reduce very greatly the volume of work in the Department and in many of the companies in arriving at year-end values. Another reason put forward was that central, provincial and state governments had assumed increasing responsibility for municipal financing in all three countries and that this has tended to raise the status of these securities. Also, it was observed that there had been some very sharp, temporary changes in the market values of corporate securities and shares in recent years and that the market price at any one point of time does not necessarily reflect the intrinsic soundness of the securities or shares. The use of an average of three year-end market values, it was believed would give a more accurate picture of the long-term value of corporate securities and shares and would give the companies time to adjust their balance sheets to new situations.

4.21 The minority view was that any extension of amortized values was likely to inhibit trading operations because the companies, under the discipline of market values, are less likely to be concerned about realized losses on sale.

[illegible] (a) municipal securities of Germany, the United Kingdom and the United States of America and (b) securities of states of the United States should be added to the list of those securities for which amortized values are to be used, and that for all other securities and shares the average of the three most recent year-end market values should be used. It was suggested that the use of amortized values for municipal securities would reduce very greatly the volume of work in the Department and in many of the companies in arriving at year-end values. Another reason put forward was that central, provincial and state governments had assumed increasing responsibility for municipal financing in all three countries and that this has tended to raise the status of these securities. Also, it was observed that there had been some very sharp, temporary changes in the market values of corporate securities and shares in recent years and that the market price at any one point of time does not necessarily reflect the intrinsic soundness of the securities or shares. The use of an average of three year-end market values, it was believed would give a more accurate picture of the long-term value of corporate securities and shares and would give the companies time to adjust their balance sheets to new situations.

4.21 The minority view was that any extension of amortized values was likely to inhibit trading operations because the companies, under the discipline of market values, are less likely to be concerned about realized losses on sale.

4.22 The federal authorities were disposed not to ease the 15 per cent common stock limit or alter the valuation provisions at that time. Their decision was to some extent tied in with their willingness to remove the limits on common stocks and income-producing real estate for segregated funds.

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

LIFE INSURANCE ASSETS IN CANADA

4.23 Assets held for the protection of life insurance policyholders and annuitants in Canada totalled $8-1/4 billion at the end of 1960 (see Table 3.k).

4.24 The total assets of the Canadian federally-registered companies amounted to $8.6 billion. As mentioned previously, of this total $2.9 billion were held outside Canada for the protection of policy-holders and annuitants abroad; the remaining $5.7 billion were held in Canada. Assets held in Canada by United States, British and other European companies against their life insurance operations here amounted to $2.3 billion. Thus, total life insurance assets held in Canada by the federally-registered companies were $8.0 billion. The total for provincial companies was $250 million.

4.25 Table 4.c shows the growth in the assets of the federally-registered companies since 1935 and analyses those assets by broad investment categories.

Table 4.c

Life Insurance Assets Held in Canada by Federally-Registered Companies

(000,000 omitted)

End of Year	Bonds	Stocks	Mortgage Loans	Real Estate	Policy Loans	Cash	Other Assets[x]	Total
1935	$ 918**	$ 158	$ 348	$ 76	$ 239	$ 26	$ 63	$1,828
1940	1,317	179	351	77	210	26	60	2,220
1945	2,222	101	280	36	152	28	67	2,886
1950	2,710	131	769	58	178	50	101	3,997
1951	2,707	131	978	69	199	43	109	4,236
1952	2,791	143	1,111	97	213	49	118	4,522
1953	2,902	153	1,297	110	225	40	131	4,858
1954	3,040**	174	1,519	135	240	35	83	5,226
1955	3,052**	206	1,812	157	250	36	86	5,599
1956	3,078**	221	2,120	183	270	41	96	6,009
1957	3,257**	215	2,367	223	295	47	107	6,511
1958	3,393**	235	2,529	250	305	54	167*	6,933
1959	3,625**	241	2,787	267	323	42	189*	7,474
1960	3,876**	246	3,011	285	344	49	196*	8,007

[x]The 1954 and later figures for "Other Assets" are on a revised basis due to changes in the annual statement form.

*Includes life companies' own stock purchased under mutualization plans.

**The breakdown for bonds can be provided only for 1935 and 1954 and later years. Data required for the analysis for the years 1936-53 are not readily available:

	1935	1954	1955	1956	1957	1958	1959	1960
Gov't of Canada	$ 273	$ 840	$ 783	$ 598	$ 538	$ 557	$ 617	$ 699
Provincial	222	354	354	389	415	414	462	526
Municipal-Canadian	205	328	374	399	427	456	507	547
Corporate-Canadian	150	1,407	1,449	1,600	1,749	1,858	1,924	1,983
Foreign	68	111	92	92	128	108	115	121
	$ 918	$3,040	$3,052	$3,078	$3,257	$3,393	$3,625	$3,876

LIFE INSURANCE ASSETS IN CANADA

4.23 Assets held for the protection of life insurance policyholders and annuitants in Canada totalled $8-1/4 billion at the end of 1960 (see Table 3.k).

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4.25 Table 4.c shows the growth in the assets of the federally-registered companies since 1935 and analyses those assets by broad investment categories.

Table 4.c

Life Insurance Assets held in Canada by Federally-Registered Companies
($000,000 omitted)

End of [illegible]	[illegible]	[illegible]	Mortgage [illegible]	Real [illegible]	Policy [illegible]	[illegible]	Other [illegible]*	[illegible]
1935	$ 918**	$ 158	$ 543	$ 76	$ 233	$ 96	$ 63	$1,823
1940	1,317	179	351	77	210	25	60	2,240
1945	2,222	101	280	36	152	28	67	2,805
1950	2,710	131	769	58	178	50	101	3,997
1951	2,707	131	978	69	199	43	109	4,235
1952	2,731	142	1,111	97	213	49	118	[illegible]
1953	2,902	153	1,207	110	225	40	131	4,878
1954	3,040**	174	1,519	135	240	35	83	5,226
1955	3,052**	206	1,912	157	250	36	86	5,699
1956	3,078**	221	2,120	133	270	41	96	6,009
1957	3,257**	215	2,357	220	295	47	107	6,511
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
1959	3,625**	241	2,797	207	323	42	189*	7,474
1960	3,876**	246	3,011	285	344	49	196*	8,007

*The 1954 and later figures for "Other Assets" are on a revised basis due to changes in the annual statement form.

[illegible]

**The breakdown for bonds can be provided only for 1935 and 1954 and later years. Data required for the analysis for the years 1936-53 are not readily available:

	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Gov't of Canada	$ 273	$ 340	$ 763	$ 598	$ 538	$ 757	$ 617	$ 659
Provincial	228	354	354	369	415	414	462	595
Municipal-Canadian	205	328	374	399	407	456	507	[illegible]
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Foreign	68	111	92	92	128	103	115	121
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

4.26 The average annual rate of growth for each five-year period since 1935 has been increasing. This is set forth in Table 4.d.

Table 4.d

Growth of Life Insurance Assets Held in Canada

(Federally-Registered Companies)

Period	Increase in Assets (000,000)	Rate of Annual Increase
1936-40	$ 392	4.0 %
1941-45	666	5.4
1946-50	1,111	6.7
1951-55	1,602	7.0
1956-60	2,408	7.4
Total	$ 6,179	6.1

4.27 Table 4.e shows the net change in invested assets by category for these 5-year periods.

Table 4.e

Net Change in Invested Assets Held in Canada

(Federally-Registered Companies)

(000,000 omitted)

	1936-40	1941-45	1946-50	1951-55	1956-60
Bonds	$ 399	$ 905	$ 488	$ 342	$ 824
Stocks	21	- 78	30	75	40
Mortgage Loans	3	- 71	489	1,043	1,199
Real Estate	1	- 41	22	99	128
Policy Loans	- 29	- 58	26	72	94
Cash	-	2	22	- 14	13
Change in Invested Assets	$ 395	$ 659	$ 1,077	$ 1,617	$ 2,298

4.28 In the period 1936 to 1940, the net increase in the life insurance companies' investments went mainly into bonds, as other types of investment were either not available in sufficient quantity or were not regarded as suitable from a quality viewpoint. The relative inactivity in the construction field is reflected in the minor changes in the mortgage and real estate categories. There was some reduction in the high level of policy loans that were outstanding as a result of the depression.

4.29 The years 1941 to 1945 reflect the channelling of not only new funds but also repayments on account of all other categories into war loans.

[illegible] interesting. This is set forth in Table 4.d.

Table 4.d

[illegible]

[illegible]

Years	Increase in Assets (000,000)	Rate of Annual Increase
1936-40	$ 392	[illegible]
1941-45	656	5.4
1946-50	1,111	6.7
1951-55	1,602	7.0
1956-60	2,408	7.4
Total	$ 6,179	6.1

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Table 4.e

Net Change in Invested Assets Held in Canada

[illegible]

(000,000 omitted)

	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Bonds	$ 395	$ 205	$ 488	$ 342	$ 524
Stocks	21	- 78	30	75	40
Mortgage Loans	3	- 71	409	1,043	1,199
Real Estate	1	- 41	22	99	128
Policy Loans	- 29	- 58	16	72	94
Cash	-	2	22	- 14	12
[illegible] Assets	$ 391	$ 559	$ 1,077	$ 1,617	$ 2,298

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4.29 The years 1941 to 1945 reflect the channelling of not only new funds [illegible]

In 1945 bond investments accounted for 77% of assets while mortgages had fallen to 10%. Figures are not available showing the Government of Canada bonds held in Canada by the life insurance companies during the war period. However, other figures will illustrate the extent of the companies' war-financing. At the end of 1939 the Canadian companies held $269 million in federal government bonds - 18% of their Canadian assets. By the end of 1946 these figures had risen to $1,229 million and 54% respectively. Government of Canada bonds held by all life insurance companies rose from $525 million at the end of 1939 to $2,265 million at the end of 1946.

4.30 During the post-war periods, although new funds have been channelled into all categories of invested assets, the emphasis placed on mortgage loans and in the last two periods on real estate is apparent in Table 4.e as the companies have endeavoured to regain a larger measure of diversification.

4.31 Changes in the percentage distribution of assets is shown in Table 4.f.

Table 4.f

Life Insurance Assets Held in Canada by Federally-Registered Companies
Percentages in Various Categories

End of Year	Bonds	Stocks	Mortgage Loans	Real Estate	Policy Loans	Cash	Other Assets	Total
1935	50.1**	8.7	19.0	4.2	13.1	1.4	3.5	100.0
1940	59.3	8.0	15.8	3.5	9.5	1.2	2.7	100.0
1945	77.0	3.5	9.7	1.2	5.3	1.0	2.3	100.0
1950	67.8	3.3	19.2	1.5	4.5	1.2	2.5	100.0
1951	63.9	3.1	23.1	1.6	4.7	1.0	2.6	100.0
1952	61.7	3.2	24.6	2.1	4.7	1.1	2.6	100.0
1953	59.7	3.2	26.7	2.3	4.6	.8	2.7	100.0
1954	58.2**	3.3	29.1	2.5	4.6	.7	1.6	100.0
1955	54.5**	3.7	32.4	2.8	4.5	.6	1.5	100.0
1956	51.2**	3.7	35.3	3.0	4.5	.7	1.6	100.0
1957	50.0**	3.3	36.4	3.4	4.5	.8	1.6	100.0
1958	48.9**	3.4	36.5	3.6	4.4	.8	2.4*	100.0
1959	48.5**	3.2	37.3	3.6	4.3	.6	2.5*	100.0
1960	48.4**	3.1	37.6	3.6	4.3	.6	2.4*	100.0

* Includes life companies' own stock purchased under mutualization plans.

** The breakdown for bonds is available only for the following years:

	1935	1954	1955	1956	1957	1958	1959	1960
Gov't of Canada	14.9	16.1	14.0	10.0	8.3	8.0	8.3	8.7
Provincial	12.1	6.8	6.3	6.5	6.4	6.0	6.2	6.6
Municipal - Canadian	11.2	6.3	6.7	6.6	6.5	6.6	6.8	6.8
Corporate - Canadian	8.2	26.9	25.9	26.6	26.8	26.8	25.7	24.8
Foreign	3.7	2.1	1.6	1.5	2.0	1.5	1.5	1.5
	50.1	58.2	54.5	51.2	50.0	48.9	48.5	48.4

LIFE INSURANCE COMPANY INVESTMENT FLOWS

Acquisitions

4.32 Table 4.b. shows the volume, trend and derivation of life insurance saving in Canada for the period 1950-60. In order to show the other side of the coin, namely, the investment activities of the industry in Canada during the period, it has been necessary to adopt the device of the statistical sample. The following material is based on a study of the life insurance companies that have reported their investment transactions to the Association since 1952 for transmission to the Bank of Canada. In 1960 these companies accounted for 76 per cent of the assets held in Canada by all companies. The broad trends evident in the investment operations of these companies, we believe, are representative of the industry as a whole and the sample is sufficiently large and representative to permit broad judgments to be made of the relationship of the life insurance industry to the financial system.

4.33 Table 4.g portrays the acquisition of new Canadian investments by this group of companies since 1951. These figures are about as close a measure of the gross investment activities of the industry in Canada as available data permit.

4.34 Even this measure of life insurance company investment activities has certain important limitations. Acquisition data include Treasury Bills and other short-term paper which may be turned over several times in the course of a year. This tends to overstatement. There also exists some variation in the companies' reporting

LI[illegible] INSURANCE COMP[illegible]

[illegible]

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methods which, in effect, may cause certain non-cash items to be included in the figures. Another qualification is the inclusion of exchanges of one form of security for another of the same issuer on a negotiated basis and similar doublt-counting arises with regard to renegotiated mortgage commitments.

4.35 Despite these several limitations, an examination of the industry's investment activities from this viewpoint does permit the formation of a more rounded appreciation of the magnitude of its involvement in the various segments of the capital market.

4.36 The development and growth of the money market in Canada during the 1950's greatly increased the participation by the companies in the short-term market. Although during the period the industry substantially reduced its holdings in Government of Canada securities (see Table 5.k), the data in Table 4.g indicate that particularly from 1954 on there were substantial acquisitions also.

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4.76 The development and growth of the money market in Canada during the 1950's greatly increased the participation by the companies in the short-term market. Although during the period the industry substantially reduced its holdings in Government of Canada securities (see Table 5.k), the data in Table 4.g indicate that particularly from 1954 on there were substantial acquisitions also.

Table 4.g

Gross Acquisitions of New Canadian Investments

(12 Companies holding 76% of Life Insurance Assets in Canada)

(000,000 omitted)

Category of Investment	1952	1953	1954	1955	1956
Gov't of Canada Securities *	$ 30.4	$ 45.4	$331.2	$282.9	$271.6
Provincial Bonds *	41.1	26.8	72.2	46.0	54.0
Municipal Bonds *	33.1	25.2	31.3	42.9	48.3
Corporate & Other Bonds	171.8	227.9	173.9	130.1	236.7
Preferred & Common Stocks	7.2	8.7	6.0	12.7	8.2
Mortgage Loans	220.7	273.0	357.1	443.2	478.6
Real Estate	16.8	15.7	29.7	28.9	30.5
Policy Loans	49.1	51.0	55.6	54.4	61.8
TOTAL	$570.2	$673.7	$1,057.0	$1,041.1	$1,189.7

	1957	1958	1959	1960	1961
Gov't of Canada Securities *	$160.5	$552.6	$328.8	$361.8	$328.8
Provincial Bonds *	54.7	33.2	62.4	84.2	140.7
Municipal Bonds *	34.8	37.0	53.2	51.1	66.8
Corporate & Other Bonds	183.5	200.6	208.9	245.2	275.2
Preferred & Common Stocks	10.3	10.5	13.7	10.0	32.0
Stock purchased for Mutualization	-	65.1	43.1	13.2	11.3
Mortgage Loans	397.4	372.7	446.3	468.2	542.4
Real Estate	45.8	32.8	22.5	30.1	18.9
Policy Loans	71.0	66.2	70.7	77.7	77.7
TOTAL	$958.0	$1,370.7	$1,249.6	$1,341.5	$1,493.8

Source - C.L.I.O.A.

* Includes guaranteed bonds.

4.37 During the period the life companies' purchase of provincial and municipal bonds was relatively stable from year to year until 1959 when the volume of purchases began to show an increase. The normal determinants of this investment are the interest rates available in this area relative to other forms of bond investment, call provisions, the availability or volume of new offerings and the credit standing of the individual borrowers.

4.38 During the period corporate bonds were purchased in relatively large amounts. Again no clear trend is apparent although, as with the provincial and municipal categories, buying increased notably since 1959. Relative attractiveness in terms of yield, availability and credit standing determine the industry's approach to this area of the market as well.

Net Investment Transactions

4.39 During the period reviewed in Table 4.g total acquisitions by these companies tended to aggregate about three times the value of total net investment. If purchases of federal government debt are excluded, since they include substantial turnover in the short-term market, a more meaningful measure of the relationship between gross purchases and net new investment to the medium- and long-term markets may be obtained. This is indicated in Table 4.h.

Table 4.h

Gross Acquisitions of New Canadian Investments related to Net Canadian Investment

(12 Companies holding 76% of Life Insurance Assets in Canada)

	A	B	C		
Year	Total Acquisitions (000,000)	Total Acquisitions excluding Federal Governments (000,000)	Total Net Investment (000,000)	A/C	B/C
1952	$ 570	$ 540	$ 220	2.6	2.4
1953	674	629	265	2.7	2.4
1954	1,057	726	284	3.7	2.5
1955	1,041	758	335	3.1	2.3
1956	1,190	918	356	3.3	2.6
1957	958	798	314	3.1	2.5
1958	1,366	813	351	3.9	2.3
1959	1,250	920	415	3.0	2.2
1960	1,341	979	432	3.1	2.3
1961	1,494	1,165	499	3.0	2.3

4.40 Net investment transactions by twelve of the major companies in Canada for each of the years 1952-61 are shown in Table 4.i. This table displays the net flow of funds quarter by quarter into the main investment categories. The predominant position occupied by the mortgage market as an outlet for net new money is illustrated in Table 4.j. During the period the major companies channeled between 50% and 85% of new funds into this category. Bonds which were the next most important area of net new investment are also shown.

Table 4.i

Net Canadian Investment Transactions
Major Categories

(12 Companies holding 76% of Life Insurance Assets in Canada)

(000,000 omitted)

Year and Quarter		Bonds	Mortgages	Stocks	Real Estate	Policy Loans	Total Net Investment
1952	I	$ 34.5	$13.6	$ - .8	$ 4.3	$ 2.9	$ 54.5
	II	28.9	22.8	1.2	4.9	4.1	61.9
	III	3.0	38.0	- .2	3.9	3.2	47.9
	IV	13.7	37.8	.1	2.3	1.5	55.4
		80.1	112.2	.3	15.4	11.7	219.7
1953	I	58.1	25.2	- 1.6	2.6	2.2	86.5
	II	8.8	36.5	2.3	3.6	3.1	54.3
	III	20.2	42.3	- .5	4.0	2.8	68.8
	IV	.8	46.5	1.7	4.0	2.0	55.0
		87.9	150.5	1.9	14.2	10.1	264.6
1954	I	36.1	29.9	- 1.5	3.0	3.0	70.5
	II	9.0	42.6	- .8	7.2	3.8	61.8
	III	- 7.4	70.0	- 2.4	7.2	3.0	70.4
	IV	- 9.8	77.8	1.5	9.7	2.3	81.5
		27.9	220.3	- 3.2	27.1	12.1	284.2
1955	I	15.5	50.3	.9	10.3	2.4	79.4
	II	14.8	56.6	- 1.2	4.9	2.6	77.7
	III	-19.2	96.4	- 2.5	7.2	1.9	83.8
	IV	5.5	81.5	4.0	1.9	1.2	94.1
		16.6	284.8	1.2	24.3	8.1	335.0
1956	I	50.5	49.6	.4	4.8	2.7	108.0
	II	- 8.7	61.0	1.6	8.5	5.4	67.8
	III	-19.1	95.2	- .4	4.6	4.7	85.0
	IV	- 2.9	86.7	- .4	8.3	3.7	95.4
		19.8	292.5	1.2	26.2	16.5	356.2
1957	I	33.8	45.7	1.4	3.9	5.4	90.2
	II	5.9	52.5	- .1	14.1	5.6	78.0
	III	- 2.1	63.1	- .7	6.7	4.9	71.9
	IV	7.2	46.0	2.0	16.7	2.8	74.7
		44.8	207.3	2.6	41.4	18.7	314.8

Sources: C.L.I.O.A.

(continued)

Table 4.i (continued)

Net Canadian Investment Transactions
Major Categories

(12 Companies holding 76% of Life Insurance Assets in Canada)

(000,000 omitted)

Year and Quarter		Bonds	Mortgages	Stocks Other	Stocks Own*	Real Estate	Policy Loans	Total Net Investment
1958	I	$71.0	$ 13.8	$ 1.0	--	$ 6.3	$ 2.6	$ 94.7
	II	19.2	29.4	.4	$44.0	7.6	2.7	103.3
	III	- 4.6	48.6	- .7	3.1	6.4	2.6	55.4
	IV	15.8	57.5	2.6	13.5	7.7	.1	97.2
		101.4	149.3	3.3	60.6	28.0	8.0	350.6
1959	I	102.1	15.0	1.6	.9	2.4	1.1	123.1
	II	16.6	56.6	1.6	22.0	2.8	1.9	101.5
	III	12.2	76.7	.9	14.8	3.8	5.4	113.8
	IV	- 6.5	65.7	- .4	4.9	6.5	6.4	76.6
		124.4	214.0	3.7	42.6	15.5	14.8	415.0
1960	I	74.4	30.0	- .6	1.3	7.0	6.4	118.5
	II	30.4	56.3	3.0	-	5.6	5.8	101.1
	III	34.2	62.5	.7	7.8	5.2	4.3	114.7
	IV	16.8	71.1	2.0	3.4	1.7	2.3	97.3
		155.8	219.9	5.1	12.5	19.5	18.8	431.6
1961	I	93.9	37.7	5.1	.1	5.6	3.2	145.6
	II	25.9	62.4	7.2	-	2.1	3.8	101.4
	III	24.6	71.2	4.6	7.8	2.5	3.2	113.9
	IV	37.6	89.8	2.5	3.4	2.2	2.4	137.9
		182.0	261.1	19.4	11.3	12.4	12.6	498.8

Source: C.L.I.O.A.

* Own stock purchased for mutualization. The differences between the 1958, 1959 and 1960 totals and those in Table 4.g are accounted for in the main by non-cash transactions.

Table 4.j

Net Canadian Investment Transactions - Bonds & Mortgages
(12 Companies holding 76% of Life Insurance Assets in Canada)

Year	Total Net Investment (000,000)	Net Investment in Mortgages (000,000)	% Mortgages to Total	Net Investment in Bonds (000,000)	% Bonds to Total
1952	$ 220	$ 112	50.9	$ 80	36.4
1953	264	150	56.8	88	33.3
1954	284	220	77.5	28	9.9
1955	335	285	84.8	16	4.8
1956	356	292	82.0	20	5.6
1957	315	207	65.9	45	14.3
1958	351	149	42.5	101	28.8
1959	415	214	51.6	124	29.9
1960	432	220	50.9	155	35.9
1961	499	261	52.3	182	36.5

4.41 Net investment in bonds has followed a definite pattern during the period. Between 1952 and 1955 the amount of net investment in bonds by the companies showed an 80% decline. However, since 1957 net investment in this area has shown a marked increase. It should be noted, however, that this category encompasses all forms of bonds, including short-term Canadas. The movement within the "Bonds" category is shown in Table 4.k.

Table 4.k

Net Canadian Investment Transactions
Classes of Bonds

(12 Companies holding 76% of Life Insurance Assets in Canada)

(000,000 omitted)

Year and Quarter		Gov't of Canada	Provincials	Municipals	Other	Total
1952	I	$ - 10.4	$ 13.1	$ 8.9	$ 22.9	$ 34.5
	II	- 7.9	4.3	5.7	26.8	28.9
	III	- 5.1	- 5.0	3.5	9.6	3.0
	IV	- 25.3	6.5	3.9	28.6	13.7
		- 48.7	18.9	22.0	87.9	80.1
1953	I	- 18.4	3.7	3.8	69.0	58.1
	II	- 16.9	- 6.3	1.4	30.6	8.8
	III	- .1	6.7	3.8	9.8	20.2
	IV	- 8.9	- 2.9	1.7	10.9	.8
		- 44.3	1.2	10.7	120.3	87.9
1954	I	- 12.8	10.6	4.3	34.0	36.1
	II	- 41.6	16.9	5.0	28.7	9.0
	III	- 22.5	- 7.4	5.5	17.0	- 7.4
	IV	- 19.8	- 4.9	2.1	12.8	- 9.8
		- 96.7	15.2	16.9	92.5	27.9
1955	I	- 6.6	9.6	5.5	7.0	15.5
	II	- 9.7	- 2.8	2.0	25.3	14.8
	III	- 3.3	- 5.1	3.3	-14.1	-19.2
	IV	- 19.9	- 2.8	11.7	16.5	5.5
		- 39.5	- 1.1	22.5	34.7	16.6
1956	I	- 40.0	5.2	6.1	79.2	50.5
	II	- 60.5	7.0	14.4	30.4	- 8.7
	III	- 23.8	.7	3.5	.5	-19.1
	IV	- 27.7	4.8	4.2	15.8	- 2.9
		-152.0	17.7	28.2	125.9	19.8
1957	I	- 12.1	6.5	8.9	30.5	33.8
	II	- 11.7	- 5.1	- 1.8	24.5	5.9
	III	- 5.9	- 4.8	.9	7.7	- 2.1
	IV	- 21.7	13.5	5.3	10.1	7.2
		- 51.4	10.1	13.3	72.8	44.8

Source: C.L.I.O.A.

(continued)

Table 4.k (continued)

Net Canadian Investment Transactions
Classes of Bonds

(12 Companies holding 76% of Life Insurance Assets in Canada)

(000,000 omitted)

Year and Quarter		Gov't of Canada	Provincials	Municipals	Other	Total
1958	I	$ 38.8	$ - 1.1	$ 4.6	$ 28.7	$ 71.0
	II	- 5.9	- 4.3	2.3	27.1	19.2
	III	- 14.4	- 5.4	- 1.1	16.3	- 4.6
	IV	9.3	7.1	9.3	- 9.9	15.8
		27.8	- 3.7	15.1	62.2	101.4
1959	I	30.2	12.6	12.0	47.3	102.1
	II	9.4	- 1.5	7.7	1.0	16.6
	III	1.4	19.9	6.8	-15.9	12.2
	IV	- 9.1	5.5	5.2	- 8.1	- 6.5
		31.9	36.5	31.7	24.3	124.4
1960	I	21.7	1.9	7.4	43.4	74.4
	II	- 8.0	23.6	7.8	7.0	30.4
	III	3.3	16.4	8.3	6.2	34.2
	IV	40.1	- 6.3	- .8	-16.2	16.8
		57.1	35.6	22.7	40.4	155.8
1961	I	15.3	42.5	16.0	20.1	93.9
	II	-10.8	16.6	- .1	20.2	25.9
	III	- .3	7.1	6.7	11.1	24.6
	IV	-15.8	33.5	13.1	6.8	37.6
		-11.6	99.7	35.7	58.2	182.0

Source: C.L.I.O.A.

4.42 During the period the life insurance companies were net sellers of Government of Canada bonds in every year except 1958-60, net buyers of municipal and corporate bonds in every year and net buyers of provincial bonds in every year except 1955 and 1958. The purpose behind this shift was to increase yield and gain diversification by category and geographically. Net investment in real estate increased in importance until 1957 but since that time has shown a significant decline.

4.43 Net increases in share holdings year by year absorbed an insignificant portion of net available funds. However, since 1955 a gradual increase in net new investments in this area has occurred. The year 1961 showed a significant increase in stock purchases. In 1957 legislation was enacted to enable a Canadian life insurance company to mutualize and a portion of investable funds has since been used for this purpose. This is shown in table 4.1 for the period 1958-61.

4.44 Throughout the period, policy loans have not required the use of a significant percentage of net available funds - not more than 5 per cent on the average. It appears that the principal determinant here is the degree of tightness in the credit environment. Tight money conditions have been accompanied by utilization of the contractual right of policyholders to take policy loans although the relatively minor movement suggests that policyholders use this avenue of credit as a last resort.

Flow of Funds for Investment in Canada

4.45 Table 4.1 illustrates the make-up of the net new funds available for investment in Canada during the period. It attempts to isolate two important elements - transfers from abroad and policy loans. No particular trend is apparent in the transfer series. During the 10 years under review, however, these transfers have amounted to between 6 per cent and 15 per cent of net new funds invested in Canada. The year 1956 was an exception when transfers from abroad accounted for 23 per cent. This may have been due to the trend toward greater strength

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in the Canadian dollar at that time, the existence of large mortgage commitments in Canada and higher yield spreads between Canadian and United States securities relative to 1955.

4.46 The only autonomous demand factor affecting the disposition of new investment funds is the exercise by policyholders of their contractual right to borrow, but in the period under review they have absorbed a relatively unimportant percentage of total funds invested.

PROPORTION OF CAPITAL NEEDS MET BY THE LIFE INSURANCE INDUSTRY

4.47 The life insurance industry is responsible for channelling a large fraction of Canadian saving to meet the capital needs of the Canadian economy and in doing so is an active participant in most segments of the capital market.

Table 4.1

Flow of Funds for Investment in Canada

(12 Companies holding 76% of Life Insurance Assets in Canada)

(000,000 omitted)

Year and Quarter		Total Net Investment in Canada	Less Transferred from Abroad	Less Increase in Policy Loans	Net Flow
1952	I	$54.5	$ 2.6	$ 2.9	$ 49.0
	II	61.9	8.7	4.1	49.1
	III	47.9	+ 1.3	3.2	46.0
	IV	55.4	5.9	1.5	48.0
		219.7	15.9	11.7	192.1
1953	I	86.5	+ 1.9	2.2	86.2
	II	54.3	6.4	3.1	44.8
	III	68.8	5.9	2.8	60.1
	IV	55.0	1.0	2.0	52.0
		264.6	11.4	10.1	243.1
1954	I	70.5	.1	3.0	67.4
	II	61.8	3.8	3.8	54.2
	III	70.4	8.1	3.0	59.3
	IV	81.5	10.9	2.3	68.3
		284.2	22.9	12.1	249.2
1955	I	79.4	5.0	2.4	72.0
	II	77.7	5.6	2.6	69.5
	III	83.8	6.7	1.9	75.2
	IV	94.1	18.2	1.2	74.7
		335.0	35.5	8.1	291.4
1956	I	108.0	27.5	2.7	77.8
	II	67.8	+ .7	5.4	63.1
	III	85.0	20.2	4.7	60.1
	IV	95.4	35.5	3.7	56.2
		356.2	82.5	16.5	257.2
1957	I	90.2	12.5	5.4	72.3
	II	78.0	7.3	5.6	65.1
	III	71.9	.9	4.9	66.1
	IV	74.7	+ .2	2.8	72.1
		314.8	20.5	18.7	275.6
1958	I	94.7	10.3	2.6	81.8
	II	103.3	26.7	2.7	73.9
	III	55.4	+ 10.8	2.6	63.6
	IV	97.2	5.5	.1	91.6
		350.6	31.7	8.0	310.9
1959	I	123.1	7.2	1.1	114.8
	II	101.5	8.8	1.9	90.8
	III	113.8	10.5	5.4	97.9
	IV	76.6	4.7	6.4	65.5
		415.0	31.2	14.8	369.0
1960	I	118.5	10.9	6.4	101.2
	II	101.1	29.6	5.8	65.7
	III	114.7	14.2	4.3	96.2
	IV	97.3	6.2	2.3	88.8
		431.6	60.9	18.8	351.9

Source: C.L.I.O.A.

(continued)

Table 4.1 (continued)

Year and Quarter		Total Net Investment in Canada	Less Transferred from Abroad	Less Increase in Policy Loans	Net Flow
1961	I	$145.6	$16.2	$ 3.2	$126.2
	II	101.4	7.5	3.8	90.1
	III	113.9	8.8	3.2	101.9
	IV	137.9	15.8	2.4	119.7
		498.8	48.3	12.6	437.9

Source: C.L.I.O.A.

4.48 The importance of mortgages in the insurance companies' investment operations has been commented upon. Table 4.m provides another measure of the importance of the part played by the life insurance industry in the financing of housing.

Table 4.m

Life Insurance Company Participation in Residential Mortgages

(000,000 omitted)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Lending Approvals For Residential Mortgages (1)	$468	$550	$816	$1,075	$877	$902	$1,407	$1,234	$938	$1,358
Lending Approvals by Life Companies	$313	$368	$453	$ 504	$495	$308	$ 432	$ 447	$458	$ 600
% Participation	67	67	56	47	56	34	31	36	49	44

Sources: Bank of Canada Statistical Summary and Canadian Housing Statistics, C.M.H.C.

(1) Total approvals for residential mortgages is the sum of total mortgage loans approved by lending institutions and C.M.H.C. on new non-farm residential construction and all mortgage loans approved by lending institutions on existing non-farm residential property.

4.49 Although the percentage participation has declined from 67% to 44% between 1952 and 1961 and reached a low of 31% in 1958, the amount invested annually has increased from just over $300 million to about $600 million. The significant fact here is that the contribution the industry has made and continues to make is a vital one without which many housing units would not be financed and the home building industry would be severely handicapped to the detriment of the economy. The decline in the industry's relative participation only

illustrates the fact that the industry's funds available for residential mortgage lending have not been able to keep pace with the total lending activity desired as is reflected in the total approvals.

4.50 A measure of the industry's investment contribution to two areas of the public sector of the economy is provided in Tables 4.n and 4.o which illustrate the degree of participation by the life insurance industry in the borrowings of the provincial and municipal governments. Capital needs served by investment in the securities of provincial and municipal governments include schools, roads, highways, utilities and other services of community living.

Table 4.n

Life Insurance Company Participation in Provincial Bond Issues

(000,000 omitted)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Net New Issues of Provincial Direct & Guaranteed(1)	$253	$160	$246	$260	$348	$505	$470	$329	$459	$924
Net Purchases by Life Companies(2)	$ 24	$ 2	$ 19	$ -1	$ 23	$ 13	$ -5	$ 48	$ 47	$132
% Participation	10	1	8	-	7	3	-	15	10	14

Sources: (1) New Issue Data - Bank of Canada Statistical Summary.

(2) Figures in Table 4.k adjusted on the basis of the premium income of the group of companies as a proportion of total premium income of all federally-registered companies.

Table 4.o

Life Insurance Company Participation in Municipal Bond Issues

(000,000 omitted)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Net New Issues Municipal Direct & Guaranteed (1)	$108	$135	$222	$217	$140	$181	$208	$213	$234	$262
Net Purchases by Life Companies(2)	$ 28	$ 14	$ 21	$ 29	$ 36	$ 17	$ 20	$ 42	$ 30	$ 47
% Participation	26	10	10	13	26	9	9	20	13	18

Sources: (1) New Issue Data - Bank of Canada Statistical Summary

(2) Figures in Table 4.k adjusted on the basis of the premium income of the group of companies as a proportion of total premium income of all federally-registered companies.

4.51 Corporation bonds form the second most important group of life insurance assets. Purchases of this type of security provide Canadian industry with an important part of their new capital requirements. Participation of the insurance companies in the corporate bond market in the period 1952-61 is shown in Table 4.p.

Table 4.p

Life Insurance Company Participation in Corporate Bond Issues

(000,000 omitted)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Net New Issues Can. Corporate & "Other" Bonds(1)	$257	$275	$393	$388	$592	$576	$473	$111	$311	$205
Net Purchases by Life Cos. (2)	$110	$152	$118	$ 44	$162	$ 94	$ 81	$ 32	$ 53	$ 77
% Participation	43	55	30	11	27	16	17	29	17	38

Sources: (1) New Issue Data - Bank of Canada Statistical Summary.

(2) Figures in Table 4.k adjusted on the basis of the premium income of the group of companies as a proportion of total premium income of all federally-registered companies.

"Other" bonds form a small part of the totals and include such issues as the International Bank and foreign governments which are sold on the Canadian market intermittently.

4.52 The economy also benefits from insurance company investments in non-residential mortgages. This represents financing of a wide variety of enterprises including shopping centers, supermarkets, office buildings, hotels and small industrial plants, warehouses and stores. Much of this financing would come within the area of so-called small business. A measure of the importance of this type of investment is given below.

Table 4.q

Life Insurance Company Participation in Non-Residential Mortgages

(000,000 omitted)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Institutional Approvals of Non-Residential Mtges. (1)	$ 82	$ 89	$115	$138	$141	$104	$175	$216	$263	$298
Approvals by Life Cos. (2)	$ 52	$ 60	$ 76	$ 92	$ 94	$ 70	$ 99	$130	$131	$141
% Participation	65	67	67	67	67	67	57	60	50	47

Sources: (1) Total approvals by all lending institutions on Other Property. Canadian Housing Statistics, C.M.H.C.

(2) C.M.H.C.

4.51 Corporation bonds form the second most important group of life [illegible] Canadian industry with an important part of their new capital requirements. Participation of the insurance companies in the corporate bond market in the period 1952-61 is shown in Table 4.p.

Table 4.p

[illegible] in Corporate Bond Issues

(000,000 omitted)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Net New Issues Can. Corporate & "Other" Bonds(1)	$257	$275	$393	$388	$592	$576	$473	$111	$311	$205
[illegible] Life Cos. (2)	$110	$152	$118	$ 44	$162	$ 94	$ 80	$ 32	$ 53	$ 77
% Participation	43	55	30	11	27	16	17	29	17	38

Sources: (1) New Issue Data - Bank of Canada Statistical Summary.

(2) Figures in Table 4.k adjusted on the basis of the premium income of the group of companies as a proportion of total premium income of all federally-registered companies.

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Table 4.q

[illegible]

(000,000 omitted)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Institutional Approvals of Non-Residential Mtges. (1)	$ 82	$ 89	$115	$138	$141	$104	$175	$216	$263	$293
Approvals by Life Cos. (2)	$ 52	$ 60	$ 76	$ 92	$ 94	$ 70	$ 99	$130	$131	$141
% Participation	65	67	67	67	67	67	57	60	50	47

Sources: (1) Total approvals by all lending institutions on Other Property. Canadian Housing Statistics, C.M.H.C.

(2) [illegible]

4.53 Policy loans provide the policyholder with a source of ready credit with which to meet an emergency or to take advantage of sudden opportunity. Table 4.r attempts to gauge the relative importance of this type of loan by comparing annual changes in consumer credit outstanding with annual changes in policy loans outstanding.

Table 4.r

Life Insurance Company Policy Loans in Relation to Consumer Credit

(000,000 omitted)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Changes in Consumer Credit Outstanding(1)	$470	$369	$139	$471	$338	$ 56	$306	$434	$320	$289
Increase in Policy Loans(2)	$ 14	$ 12	$ 15	$ 11	$ 22	$ 26	$ 12	$ 19	$ 23	$ 15
%	3	3	11	2	6	46	4	4	7	5

Sources: (1) Bank of Canada Statistical Summary.

(2) Table 4.b - fourth column from right.

4.54 It will be observed that the demand for policy loans reached a peak during the period covered in Table 4.r in the year 1957 when consumer credit was in short supply. Most "permanent" life insurance contracts provide policy loan privileges and specify the rate of interest to be charged. In no case does the rate exceed 6%.

SEGREGATED FUNDS

4.55 The power of federally-registered companies to issue variable accumulation and annuity contracts was clarified in 1961. The Insurance Acts were amended to require that the funds relating to such contracts be segregated from the funds relating to the regular life insurance and annuity business of the companies. Several provincial companies have the power in their charters to issue variable contracts and one is already doing so.

4.56 The Association asked the twenty life insurance companies with the largest asset holdings in Canada to report upon their plans and progress in developing this new line of business. The group included three United States, two British and fifteen Canadian companies, which together hold 88% of life insurance assets in Canada. As at the end of March, 1962, eight of these companies had established

4.53 Policy loans provide the policyholder with a source of ready credit with which to meet an emergency or to take advantage of sudden [illegible]rtunity. Table 4.r attempts to gauge the relative importance of this type of loan by comparing annual changes in consumer credit outstanding with annual changes in policy loans outstanding.

Table 4.r

[illegible]

(000,000 omitted)

	[illegible]	1953	1954	1955	1956	1957	1958	1959	1960	1961
Changes in Consumer Credit Outstanding(1)	$470	$369	$139	$471	$338	$ 56	$306	$434	$320	$280
Increase in Policy Loans(2)	$ 14	$ 12	$ 15	$ 11	$ 22	$ 26	$ 12	$ 19	$ 23	$ 15
%	3	3	11	2	[illegible]	46	4	4	7	5

Sources: (1) Bank of Canada Statistical Summary.

(2) Table 4.b - fourth column from right.

4.54 [illegible] during the period covered in Table 4.r in the year 1957 when consumer credit was in short supply. Most "permanent" life insurance contracts provide policy loan privileges and specify the rate of interest to be charged. In no case does the rate exceed 6%.

[illegible]

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[illegible] The Association asked the twenty life insurance companies with the largest asset holdings in Canada to report upon their plans and progress in developing this new line of business. The group includes three United States, two British and fifteen Canadian companies, which together hold 66% of life insurance assets in Canada. As at the end of March, 1962, eight of these companies had established

segregated funds and seven more expected to do so during the year.

4.57 With respect to the fifteen companies that are or will shortly be in this business, thirteen are, so far, confining their activity to group contracts while two are also making individual contracts available.

4.58 All these companies sell variable accumulation contracts. These provide that the contributions will be accumulated and that the rights to benefit will depend upon the value of the assets held by the fund at the time the right is exercised. At that time the benefit may be paid out as a fixed annuity. Alternatively, a variable annuity which would provide for the payments to vary as the value of the assets in the fund varies can be sold. One company is already issuing these variable annuities and a second expects to make them available in the near future.

4.59 Six of the companies have only equities in their segregated pooled fund or funds and a group policyholder is able to divide his pension plan contributions between the equity fund and the regular annuity lines of the company. Eight companies have both segregated equity and segregated "fixed-income" funds between which the group policyholder can allocate his contributions. Three of these companies have a separate bond fund and a separate mortgage fund, the others will combine all debt-type investments in one fund.

4.60 Of the fifteen companies, twelve are prepared to set up a separate investment account for a large group policyholder. Five of these companies would permit

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4.60 Of the fifteen companies, twelve are prepared to set up a separate investment account for a large group policyholder. Five of these companies would permit

the policyholder to participate in investment decisions while six would not.

4.61 For the purpose of funding group pension plans, five companies restrict contributions to the equity fund to the employers' share and nine have no such restriction and one has as yet made no decision on the matter. Most of the companies give the employer freedom not only to vary the proportion of his plan's contributions going into equity funds from time to time but also to transfer previously deposited contributions from such funds. With regard to marketing, six companies use their existing sales force and eight use not only their own organization but also general insurance brokers, actuarial or pension consultants and others.

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SECTION 5

INVESTMENT THEORY AND PRACTICE

5.1 The theory of life insurance investment is based on the nature of the liabilities assumed - the commitments to pay claims and benefits as they become due and the interest guarantee given on moneys already received and moneys to be received in the future.

5.2 Life insurance companies must maintain reserves which represent the amount which together with premiums and interest to be received in the future will enable them to meet these future obligations. The great majority of life insurance and annuity contracts will run for many years before maturing and are often further extended by payment of regular amounts to beneficiaries each year. In the process a large pool of personal savings becomes available for investment in the Canadian economy.

5.3 There are nearly 9 million policyholders in Canada. It would be calamitous if a company were unable to meet its obligations under contracts on which the policyholders had paid premiums for years and upon which they have placed dependence not only for themselves but also for their families. Therefore, above all, life insurance protection must be absolutely reliable. This has been recognized in insurance legislation and in the degree of continuing supervision in Canada. It is also recognized by the companies themselves in the conduct of their own affairs.

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5.4 Security of principal, then, must be a prime consideration in the investment of life insurance funds.

Liabilities are expressed for the most part in fixed-dollar amounts and in relation to these liabilities, surplus funds, although adequate, are not large. The insurance industry must, therefore, invest its funds so that the risk of loss is minimized. This is done by investing the great preponderance of assets in fixed-dollar form, that is, in debt investments. Security of principal is obtained by careful selection of individual investments as to their credit-worthiness that is, as to their ability to pay interest and repay principal when due. It is further assured by diversification. That is, in part, obtained by distributing assets over various categories of investments (bonds, mortgages, real estate, stocks) and also by obtaining wide geographical distribution. Within each category of investment further diversification is obtained by limiting the size of individual investments. For those companies operating outside of Canada the risk of exchange loss is minimized by trying to match liabilities with assets expressed in the same currency.

5.5 The next important consideration is the investment of funds so that they will yield the largest return consistent with the required safety. The competitive nature of the life insurance industry compels this. Not only must the companies earn a net rate of interest at least equal to the rate assumed for premium and reserve computations but also they must try to earn the highest possible mergin over and above that rate so that the cost of insurance to policy-holders may be as low as possible. Companies, therefore, are

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extremely sensitive to yields obtainable in the capital market and will accordingly vary the direction of their investment programs in order to obtain the highest possible net return on their assets.

5.6 Experience has shown that with the growth of the industry cash demands by policyholders which may arise either through the withdrawal of funds left on deposit or the exercise of the contractual rights for policy loans and cash surrender values can be met normally by the industry's net cash inflow. A sudden increase in demands by policyholders for cash is more likely to have its impact on investment policy by limiting the amount available for new investment than by forcing the sale of assets. This allows the companies to maintain fully invested positions and places little emphasis on any very high degree of liquidity for this reason.

5.7 The life insurance companies in Canada, of course, must invest their assets within the framework of restrictions and limitations imposed by the various Insurance Acts. While so far most of these restrictions have for their purpose the avoidance of undue risk or the limitation of economic power, they nevertheless have an important effect on the pattern of investment. For example, the Canadian market value test for non-government securities when coupled with rigidities in the valuing of liabilities tends to limit investment in securities subject to wide market fluctuations, such as common shares or perpetual bonds.

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5.8 While life insurance companies have a preference for long-term investments because of the long

term nature of their liabilities, it does not follow that their assets should be always invested in securities with very long maturities. Investing in long-term issues may provide a hedge against a fall in interest rates but it provides no assurance that the rate of return on the assets so invested will be maximized. The main debt media available with long-term maturities and possessing good protection against pre-payment are government bonds where the return is normally relatively low. The larger income usually available from other investment sources in itself can provide some hedge against a fall in interest rates. As compared with an investment in a long-term maturity, an investment in a shorter maturity will have been justified if the higher income obtained over the life of the shorter-term investment when taken in conjunction with the income on the reinvestment of the money is greater than that which would have been obtained by the immediate investment in a long-term maturity. Furthermore, an investment in very long-term corporate obligations, when available, may conflict with the objective of security of principal since in a period of rapid economic, political and technological change the credit-worthiness of an asset can alter substantially. In investing its funds, therefore, an insurance company will try to obtain the highest eventual return on its assets by tending to favour shorter-term investments when it believes interest rates are low and tending to favour longer-term investments when it believes interest rates are high, but few if any companies would follow a policy of always investing in very long-dated

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or perpetual securities.

5.9 An active investment policy is normally followed by the life insurance industry. This involves not only the shifting of investment funds into the media offering the relatively highest return but also the trading or exchanging of securities within and between classes. In order to facilitate an active investment policy, a good degree of marketability on a substantial portion of assets is important. Trading activity is not limited to actions taken in the light of changes or expected changes in political and economic conditions but also involves the buying and selling of securities to take advantage of market differentials which appear to be out of line. In following an active investment policy the life insurance companies try to improve the return on their investment portfolios and by their activities broaden the capital market by promoting a freer flow of funds between many of its sectors.

INVESTMENT PRACTICE

5.10 The following comments arise from a study of a representative cross-section of the industry in Canada. It should be noted, however, that despite the general conclusions indicated by this study there are important variations among the individual companies relating to investment practices.

Net Increase in Assets

5.11 The net increase in assets of life insurance companies is characterized by predictability, regularity and stability. The substantial growth in new business

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from year to year as experienced in the past decade has not been immediately reflected in corresponding asset growth due to the concentration of acquisition and related expense in the early years of a new policy. Mechanization has tended to modify the effect of rising costs but in itself has brought capital expenditures for equipment. Surrenders generally reflect economic conditions. On the other hand, the increase in the rate of interest earnings in the past fifteen years has had a helpful effect on the growth of assets.

5.12 The underlying stability and predictability of growth is an important reason why life insurance companies can approach their investment problem with a long-term view and can afford to make important forward commitments. The steady flow of new investible funds to the companies creates a pressure for full investment and precludes their withdrawal from investment markets for any extended period.

Reinvestment of Maturing Assets

5.13 The regular monthly repayment of principal on the large mortgage holdings of the companies produces in aggregate a substantial cash flow which in recent years has become increasingly important.

5.14 The amortization of real estate held for the production of income, the serial or annuity bonds of municipalities and the sinking fund repayments of corporation bonds, particularly thsoe directly placed, also produce regular flows of repayments for reinvestment.

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has been reduced to within three to five years they enter an area of the market where short-term investors are active and it is usually possible to sell the securities and reinvest in longer-term securities at an increase in yield.

5.16 These bonds form part of the regular flow of investible funds for new commitments. Of somewhat the same nature but lacking the same predictability is the redemption of assets. The greatest volume of redemptions occurs when high-coupon issues are refunded during periods of low interest rates. Redemption of corporate bonds prior to maturity usually is the result of the special circumstances of the borrower such as merger, sale, increased financing beyond the provisions of the existing trust deed, recapitalization or advance repayment by cash. During recent years investors have been able to protect themselves to some degree by obtaining "non-refunding" clauses in new issues, which are effective for a portion of the life of the bond.

5.17 Mortgage loans made to individuals, such as most single-family residential mortgages, are also subject to early redemption - since under provisions of the Interest Act this right is available to the borrower at the end of five years. Redemptions also frequently occur when home ownership changes hands.

5.18 Redemptions are thus quite unpredictable but characteristic of periods of falling interest rates. They can be quite substantial and have in the past produced large increases in investible funds at a time when investment opportunities were limited and interest

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rates low.

Trading *

5.19 Estimates based on an analysis of the operations of companies holding 76 per cent of assets in Canada indicate that trading, as measured by the sale of investments to make an alternative investment, approaches one and one-half times the volume of new funds invested.

5.20 It is clear that this experience varies widely between companies, due to factors of policy, practice and personnel. The ratio referred to has been about 2 - 1 in the case of one of the most active trading companies and in the case of other companies it assumes relatively small proportions. On the whole, indications are that some of the larger companies, with larger investment staffs, are relatively the more active traders. However, some larger companies that have relied more extensively on mortgage investments and placed less emphasis on security portfolios are not so active.

5.21 It is apparent from the operations of one company, which deals in Canadian, American and British securities, that a broad diversified market unhampered by special deterrents to trading, fosters the trading operation. Measuring the company's average annual securities activity (purchases and sales) relative to its securities portfolio in each market over the three-year period 1958-1960, it was found that that activity in the United States was double that in Canada and activity in Canada was double that in the United Kingdom. Although the Canadian activity is overstated because of quite large operations in short-term bonds

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and bills during the period, the order of the three markets as far as activity goes is shown by these ratios. This indicates the stimulus given to trading by the size, breadth and diversity of the United States market and the deterrent effect on trading in the London market of the 2 per cent stamp duty which limits trading very largely to government securities. It is fair to add that the additional profits available in a market conducive to trading are at least partial offet to yield differentials in considering the disposition of funds.

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Regional Diversification

5.22 The principle of diversification which has been evidenced so far in this submission involves the distribution of investment by category of asset. Implicit in this prinipcle is also diversification by geographical area. Basically, this is designed to obtain a spread of risk. At the same time, however, life insurance investment dollars are widely diffused throughout the economy. In this diffusion they supplement local funds available for local investment.

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5.23 Despite the fact that the life insurance companies are national concerns and the policyholders look to the entire pool of assets for their security, the geographical distribution of assets is quite close to the approximate distribution of liabilities on a provincial basis. This is almost diametrically opposed

to the comment so often heard that the life insurance companies withdraw savings from a particular area and invest them somewhere else.

5.24 The Commission will appreciate the difficulties involved in making this kind of a comparison. As far as the assets are concerned, provincial and municipal bonds and mortgage and real estate investment can all be directly allocated. Corporation bond and share holdings require detailed analysis and allocation on the basis of location of properties, track or pipeline mileage, bank clearings or some other appropriate basis for those corporations that operate in more than one province. Federal government obligations require distribution on the basis of population. The allocation of reserves and other liabilities to policyholders require a different set of assumptions. In the case of reserves, these assumptions differ for insurance and annuities and for individual and group forms of insurance and annuities.

5.25 Notwithstanding this, we believe that the following analysis is sufficiently accurate to be quite significant.

Table 5.a

Estimated Regional Distribution of Life Insurance Assets and Liabilities in Canada - End of 1960

(000,000 omitted)

	A Invested Assets held in Canada*	B Liabilities to Policyholders in Canada	A/B
British Columbia	$ 872	$ 565	154%
Alberta	672	425	158
Saskatchewan	243	180	135
Manitoba	362	327	111
Ontario	3,429	3,146	109
Quebec	1,910	1,901	100
New Brunswick	118	135	87
Nova Scotia	169	200	85
Prince Edward Island	19	18	106
Newfoundland	67	55	122
	$7,861	$6,952	
Non-invested assets	$ 208		
Foreign securities "held in Canada"	191		
Other liabilities		$ 415	
Excess of assets over liabilities		893	
	$8,260	$8,260	

Source: C.L.I.O.A.

*Not included are the securities of Canadian borrowers issued in Canadian dollars or other currencies and held for non-Canadian policyholders.

5.26 It should be borne in mind that these assets and liabilities will change from year to year, although not significantly, as the assets respond to investment opportunity and availability of credit-worthy investments and as the liabilities change in response to both new business and the aging of existing business.

The Average Maturity of Assets

5.27 There is considerable reference literature on the subject of matching insurance investments to relevant liabilities. This theory attracted attention first in the United Kingdom where conditions lend greater support to its practical application - for example, a larger pool of longer-dated or perpetual fixed-interest securities, relatively rigid call provisions on these securities and non-fixed cash or loan values on policies. However, even under these

conditions, evidence before the Radcliffe Commission indicated only a "broad bias" in the direction of matching liabilities with security investment "provided it meets requirements on market and investment considerations."

5.28 The Association believes that in Canada this is little more than a background consideration in investment policy and, among a selected group of representative companies approached on the subject, there were none that attempted to set up maturity schedules of assets and liabilities as a guide to investment policy.

5.29 A few companies undertake the preparation of a periodic schedule of the maturity breakdown of their bond and debenture portfolios. A study of a selection of these schedules indicates that, during the last few year, most companies have had the largest quinquennial group of maturities in the 15 to 20-year bracket and the smallest group in the 5-year and less bracket. At the end of 1960, the percentage of bond and debenture maturities falling in the former group ranged between 26.2 per cent and 30.6 per cent for the companies providing the breakdown. The range for the 5-year and less group was 7.7 per cent to 14.2 per cent.

5.30 Average term of the bond and debenture portfolios of those particular companies ranged between 12 years 11 months and 15 years 2 months at the end of 1960. Insofar as a trend could be determined from the limited data available, it appears that the average term of bond and debenture portfolios has lengthened since the mid-1950's.

5.31 No exact calculation of the average term

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of mortgage portfolios has been available, nor is it likely to be a practical calculation. Howevee, where some estimates have been available, they vary widely from roughly 5½ years in one case to over 10 years in another one. Those companies having a larger proportion of loans in apartment,commercial and industrial property categories, where the term of loan and amortization tends to be longer than for housing loans, are likely to have the longer average term on their portfolios. Insofar as a trend was indicated by available figures, it pointed to a lengthening of the average term on mortgage portfolios over the past few years.

5.32 The view has been expressed, on occasions, that the industry has exposed its policyholders to unnecessary risks by failing to invest for a term more consonant with its liabilities. It must be remembered, however, that the liabilities are extremely long-term and that, even assuming an exact calculation of the maturity of assets and liabilities was possible, it would be extremely unlikely if an insurance company could approach a reasonable balance. In the first place, the volume of really long-term investments is limited and in the second place, the terms of investment are at best a compromise between borrower and lender and where the lender desires a long or a short maturity, the borrower will by the nature of things have a strong leaning towards the converse. There will, consequently, be a pull away from the exact term sought by the lender to meet any maturity schedule.

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The Effect of Monetary Policy

5.34 The effect of monetary policy on the life insurance companies flows essentially from changing interest rate levels and relationships and although not direct is nevertheless pervasive.

5.35 The life insurance companies invest through many channels --- federal government bonds, provincial bonds, municipal bonds, corporate bonds, preferred and common stocks, N.H.A. and conventional mortgages, income-producing real estate and so on -- and thus have many points of exposure to changing interest rates. Although the investments are essentially in the long-term category, short-term bonds and commercial paper are acquired from time to time. This spectrum of investment is much wider than that normally employed by most other financial intermediaries such as trusteed pension plans, mutual funds and credit unions.

5.36 The fact that life company investments are preponderantly long-term makes them particularly susceptible to the effects of monetary policy to the extent that these effects are felt in the yields in the long-term market. Lower bond prices or higher interest rates tend to restrict the exchange of existing holdings for others of higher yields because of the magnitude of the losses

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5.36 The fact that life company investments are preponderantly long-term makes them particularly susceptible to the effects of monetary policy to the extent that the effects are felt in the yields in the long-term market. Lower bond prices or higher interest rates tend to restrict the exchange of existing holdings for others of higher yields because of the magnitude of the losses

immediately involved. Falling interest rates and rising bond prices tend to promote the exchange of securities for the purpose of either improving relative yield or, at later stages, reducing term.

5.37 As mentioned previously, each company's net earned interest rate is important in lowering the cost of insurance to its policyholders and the relative level is important as each life insurance company competes with the others and all compete with the other savings intermediaries. Thus, each company is sensitive to changing yields in the market-place as it attempts to make the most of the opportunities for profitable investment that present themselves.

5.38 Life insurance companies are responsive to change or expectation of change in interest rate levels in at least four ways: (a) the direction of the investment flow; (b) the liquidity of existing assets; (c) the generation of cash for investment; and (d) the degree of forward commitments. It should be noted, though, that these effects are produced whether or not the change in interest rate levels is induced by the monetary authority or whether the change is the result of the interplay of the normal forces of supply and demand.

5.39 For example, when an expectation of monetary ease exists or is created, investment emphasis shifts to those areas where yields are flexible and likely to decline. Longer-term assets are preferred, forward commitments are increased. As rates decline, emphasis tends to shift to those areas of investment where interest

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rates have not decreased to the same extent. During this phase as mortgage repayments increase, as existing bond investments are refunded, as more monies are left on deposit and the increased market value of investment holdings facilitate disposal of assets at smaller losses or at profits.

5.40 When monetary restraint is expected, the reverse is true. Life insurance companies are less willing to assume a fully-committed position with respect to their cash flow. Emphasis tends to be placed on either short or medium-term securities. Prepayments of existing investments tend to decline. Because of the lower market values, sale of existing assets becomes more difficult except at larger losses. Less funds tend to be left on deposit and policy loans tend to rise.

5.41 It should be noted that the same effects flow from the federalgovernment operations in the area of debt management to the extent that those operations produce variations or expected variations in the level of interest rates or relationships within the interest rate structure.

The Influence of Exchange Rates

5.42 Most life insurance companies are desirous of assuming the minimum of exchange rate risk in their investment operations. In general, the attempt is made to match foreign currency assets to foreign currency liabilities. Indeed, some foreign jurisdictions require full or substantial investment of matching assets in their own currency. (Non-resident companies doing business here are encouraged by the authorities to cover

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5.43 It is among Canada, the United States and the United Kingdom that acceptance of foreign exchange risks has been noticeable in the past.

5.44 Canadian life companies have from time to time been prepared to accept some exchange risk and to purchase non-resident investments when the differential in interest rates appeared unduly narrow. Some reversal of that position occurs when the yield spread widens appreciably.

Asset Holdings by Size of Company

5.45 The assets held in Canada by the individual Canadian companies have been analysed on a quinquennial basis back in 1935. Table 5.b shows the results of grouping the largest ten portfolios, the next largest ten and the remaining portfolios for each of the six year-ends.

5.46 In the post-war period mortgage loans would appear to represent a smaller proportion of the portfolios of the group of smallest companies than of the groups of larger companies. This presumably stems from the fact that there are "economies of scale" in a mortgage operation - the larger the flow of loanable funds the easier it is to build and maintain an efficient mortgage organization. However, the post-war pattern did not obtain in the late 1930's and early 1940's when the mortgage operations of most companies were contracting.

5.47 In the 1950's the real estate holdings of the group of smallest companies were low relative to larger companies. The acquisition of income-producing

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Table 5.b

Life Insurance Assets Held in Canada by Canadian Federally-Registered Companies

Percentages in Various Categories

(Book Values)

End of	Company Grouping	Bonds	Stocks	Mortgage Loans*	Real Estate	Policy Loans	Cash	Other Assets	Total
1935	Largest ten	39.96	12.59	23.76	5.50	13.28	1.30	3.61	100.00
	Next ten	41.34	3.81	28.11	5.00	16.01	1.08	4.65	100.00
	Remaining 7	35.48	6.07	27.16	6.57	15.23	1.95	7.54	100.00
	All Companies	40.03	11.81	24.15	5.47	13.52	1.29	3.73	100.00
1940	Largest ten	52.20	11.35	19.50	4.36	9.22	.73	2.64	100.00
	Next ten	47.32	7.16	25.41	4.23	11.04	1.60	3.24	100.00
	Remaining 8	45.55	9.71	18.29	8.76	11.18	2.21	4.30	100.00
	All Companies	51.67	10.94	20.02	4.41	9.42	.83	2.71	100.00
1945	Largest ten	73.78	4.21	12.49	1.73	5.26	.34	2.19	100.00
	Next ten	63.40	8.40	18.27	1.03	5.56	.81	2.53	100.00
	Remaining 8	68.59	9.35	9.11	2.83	5.24	1.88	3.00	100.00
	All Companies	72.60	4.74	13.05	1.67	5.29	.41	2.24	100.00
1950	Largest ten	62.32	3.13	24.80	2.04	4.48	.76	2.47	100.00
	Next ten	54.23	7.59	28.70	1.04	4.94	.94	2.56	100.00
	Remaining 10	54.30	9.30	24.73	1.38	5.38	1.56	3.35	100.00
	All Companies	61.21	3.78	25.24	1.91	4.56	.80	2.50	100.00

* Includes agreements of sale.

Table 5.b. (continued)

Life Insurance Assets Held in Canada by Canadian Federally-Registered Companies

Percentages in Various Categories

(Book Values)

End of	Company Grouping	Bonds	Stocks	Mortgage Loans*	Real Estate	Policy Loans	Cash	Other Assets	Total
1955	Largest ten	46.08	3.83	39.53	3.96	4.46	.44	1.70	100.00
	Next ten	48.35	4.06	37.39	2.29	5.50	.74	1.67	100.00
	Remaining 12	56.46	6.85	25.16	2.26	5.66	1.77	1.84	100.00
	All Companies	46.61	3.94	38.91	3.73	4.61	.51	1.69	100.00
1960	Largest ten	38.80	3.05	45.37	4.95	4.38	.49	2.96	100.00
	Next ten	45.86	2.77	40.38	3.05	5.56	.60	1.78	100.00
	Remaining 16	59.06	7.08	24.14	1.45	4.81	1.28	2.18	100.00
	All Companies	40.22	3.14	44.17	4.62	4.53	.52	2.80	100.00

* Includes agreements of sale.

real estate usually involves a sizeable investment and often a smaller company is prevented from participating because of the limitations in the law and the need for diversification of its assets.

5.48 In the post-war period the stock holdings of the smallest companies as a group are high relative to the other two groups. This result is brought about by the holdings of two or three particular comoanies that, because of their relative size, weigh heavily in the percentages for the group of smallest companies.

5.49 Within each grouping the relative proportions of bond holdings varies inversely with mortgage holdings. There appears to be no particular pattern in the case of policy loans while cash balances naturally form a larger part of the assets of smaller companies than of larger companies.

5.50 It is appropriate to emphasize at this point that the statistical aggregates and averages which of necessity are used throughout this submission tend to veil the fact that each of the life insurance companies is pursuing its own investment policy quite independently of the others. The companies compete in the capital market just as they compete in the insurance market.

5.51 Table 5.c presents some figures on the categories of assets held in Canada at the end of 1960 by individual Canadian companies. The extent of the variation between individual companies in their judgment as to portfolio management indicates that there are no built-in industry limitations other than those that each company imposes on itself as it pursues its investment

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objectives to the best of its ability.

5.52 One company had 26 per cent of its portfolio in bonds while a second company had 57 per cent of its assets in this category. The percentages for the other companies range between these two figures. For mortgage loans there was a range of nil to 64 per cent. For real estate there was a variation between nil and 10 per cent; it might be observed in this connection that the 5 per cent limitation in the law at the end of 1960 (later increased to 10 per cent) related to income-producing real estate alone and applied on the total portfolio of the companies, not the in-Canada portfolio only. For stocks the range or percentages was from nil to 12 per cent; this is based on book values which in many cases are about half of current market values.

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Table 5.c

Life Insurance Assets Held in Canada by Selected Canadian Companies - End of 1960

Companies with Highest (H) or Lowest (L) Percentages in Any Category of Asset within the Groupings by Size (see Table 5.b)

(Federally-Registered Companies' Book Values)

Company Grouping	Bonds	Stocks	Mortgage Loans*	Real Estate	Policy Loans	Other Assets	Total
Largest ten							
Company A.	46.8(H)	7.2(H)	33.0(L)	5.3	2.8(L)	4.9	100.0
B.	26.0(L)	.3	63.8(H)	2.1	5.6	2.2	100.0
C.	41.4	2.6	46.3	1.9(L)	5.8(H)	2.0	100.0
D.	38.8	.5	45.6	7.7	4.4	3.0	100.0
E.	33.6	.2(L)	46.9	10.4(H)	4.0	4.9	100.0
Next ten							
Company F.	68.7(H)	2.0	17.9(L)	3.6	5.7	2.1	100.0
G.	32.1	5.5(H)	51.6	4.3	4.1(L)	2.4	100.0
H.	50.0	2.4	35.4	.9	7.6(H)	3.7	100.0
I.	43.6	3.7	38.4	4.6(H)	5.9	3.8	100.0
J.	28.7(L)	.5(L)	64.3(H)	.1(L)	4.4	2.0	100.0
Remaining 16							
Company K.	58.9	12.5(H)	20.1	.6	5.5	2.4	100.0
L.	50.2	1.9	32.5	3.8(H)	.9	10.7	100.0
M.	43.3(L)	4.2	39.6	2.1	8.1	2.7	100.0
N.	58.6	4.2	25.8	**(L)	8.3(H)	3.1	100.0
O.	97.5(H)	**(L)	**(L)	**(L)	**(L)	2.5	100.0
P.	45.4	**(L)	52.1(H)	**(L)	**(L)	2.5	100.0

* Includes agreements of sale.

** Nil holding. These are very small or new companies.

The Influence of Relative Investment Earnings Rates

5.53 Rates of investment income earned, as reported b the individual companies in the annual statements required by the Department of Insurance are based on total invested assets. Since a number of the larger Canadian companies operate extensively outside of Canada, any average yields based on such figures would not be representative of Canadian experience.

5.54 The rates of investment income earned on Canadian assets alone have been obtained from a few representative companies. It has not been possible to weight the average yields according to the size of the individual company portfolios. Also, the data are based on different numbers of companies in certain years. Yields in the stock category are influenced by company book value adjustments to a much larger degree than the other portfolio categories. In addition, stock purchases have been made for purposes of long-term growth rather than for immediate dividend return, and even if it were possible to correct for the book value adjustments, there would still be difficulties of interpretation.

5.55 With these qualifications, the figures as shown in Tables 5.d and %.e indicate:

(a) There has been persistent improvement in gross investment return on Canadian assets in the period 1951-60; in varying degrees this applies to all categories of investment.

(b) The improvement in investment return has been more marked in the second half of the decade as a result of the increasing weight of the acquisitions of

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(a) There has been persistent improvement in gross investment return on Canadian assets in the period 1951-60; in varying degrees this applies to all categories of investment.

(b) The improvement in investment return has been more marked in the second half of the decade as a result of the increasing weight of the acquisitions of

higher-yielding assets.

(c) Since the early 1950's there has been a slight narrowing of the differential in gross investment return as between bonds and mortgages; the differential for 1960 was 1.55per cent as against 1.70 per cent for 1951. However, this is more than offset by the improvement in the expense ratio relative to mortgage business. In 1950, mortgages cost about 9/10 of 1 per cent more to administer than did securities, whereas by the end of the decade this difference has narrowed to about 1/3 of 1 per cent. Consequently, the effective spread has, in fact, increased. The improved mortgage expense ratio results largely from the growth in the mortgage portfolios.

(d) The policy loan yields reflect, a distinct lag in responding to interest rate trends. Most policy contracts provide for a loan in erest rate not in excess of 6 per cent. Their expense ratios show policy loans to be relatively costly to administer because of their small size.

(e) There has been a significant decline in the overall investment expense rate during the decade; this is largely attributable to the fact that a very much larger mortgage and realestate portfolio is being administered without major additions to overhead.

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Table 5.d

Gross Rates Of
Investment Income Earned By Some Canadian
Life Insurance Companies On Their Canadian Assets
(By Portfolio Categories)

	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960
Bonds (1)	3.40	3.53	3.70	3.82	3.85	4.01	4.10	4.33	4.59	4.74
Stocks (2)	5.81	5.78	5.74	5.65	5.95	6.14	6.08	5.80	5.74	5.87
Mortgages (1)	5.10	5.20	5.37	5.50	5.57	5.64	5.81	5.97	6.10	6.29
Real estate (3)	4.32	4.63	4.98	4.78	4.84	5.23	5.52	5.60	5.51	5.60
Policy loans (4)	4.98	4.92	5.38	5.27	5.34	5.36	5.87	5.92	5.89	5.94
Total (Gross) (2)	4.12	4.30	4.55	4.66	4.79	4.97	5.16	5.33	5.51	5.68

(1) Estimate based on results of 6 companies, 1951-53 and 7 companies, 1954-60
(2) Estimate based on results of 5 companies, 1951-53 and 6 companies, 1954-60
(3) Estimate based on results of 5 companies, 1951-53 and 6 companies, 1954-56 and 7 companies, 1957-60
(4) Estimate based on results of 3 companies, 1951-53 and 4 companies 1954-56

* * * * * *

Table 5.e

Approximate Investment Expenses in Canada By
Main Portfolio Categories (1)
(As % Of Invested Assets)

	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960
Securities	.08	.08	.09	.08	.08	.09	.09	.10	.11	.09
Mortgages	1.02	.82	.75	.57	.58	.54	.52	.46	.43	.42
Policy loans	.84	.78	.80	.85	.93	.85	.89	.84	.83	1.00
Total	.39	.39	.43	.36	.34	.33	.37	.33	.34	.34

(1) These figures are based on the investment expenses reported by a small group of companies. There is very little variation from company to company except in the case of policy loans, where there are difference in the method of apportioning expenses.

The Effect of Mutualization on Investment Operations

5.56 In December, 1957, the Canadian and British Insurance Companies Act was amended to permit Canadian companies registered under the Act to mutualize by the purchase of their own shares. The Act states that after the necessary by-laws have been approved by shareholders and participating policyholders and sanctioned by the Treasury Board a company may institute a plan to purchase its own shares. A maximum period of five years following the year of purchase is allowed for writing down shares purchased to their par value. Mutualization is not completed until this has been done and the shares have been cancelled.

5.57 Five companies are in the process of mutualization. The companies had completed purchase of their shares by the end of 1961. No company has yet completed the write-down of its stock to par. Of the five companies, four do a large amount of business outside of Canada and have substantial non-Canadian assets. Part of the money used to purchase their stock has come from assets held out of Canada.

5.58 During the period 1958-61, cost of shares purchased under the mutualization program of the five companies was $136 million against an increase in their world-wide assets, after deducting the book value of their own shares held, of $913 million. These purchases represented only 14.9 per cent of their increase in assets.

5.59 During the same period total assets in Canada of federally-registered companies, after deducting the value of any shares held as a result of mutualization,

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increased by approximately $2 billion. It is evident, therefore, that the mutualization of the five companies did not withhold any significant amount from normal investment channels and if allowance is made for the reinvestment of the moneys received by the holders of the shares acquired, the net overall effect would be negligible.

5.60 Several mutual companies have operated in Canada for many years. There is no evidence to show that their investment policy, as a result of their being mutual, differs materially from that of the stock companies. It is not anticipated that additional mutualization of the industry will result in any change in the industry's investment policy.

Holdings by Canadian and Non-Canadian Companies

561 Assets held in Canada by Canadian, British and other non-resident companies are set out in Table 5.f for the year 1960. It should be noted that the assets of the non-resident companies are shown at market values while those of the Canadian companies are at book values.

Table 5.f

Life Insurance Assets* Held in Canada by Federally-Registered Companies
End of 1960

Canadian Bonds	Canadian Companies (000,000)	%	British Companies (000,000)	%	United States and Other Companies (000,000)	%
Government of Canada	$445	7.73	$40	7.42	$214	12.40
Provincial	384	6.70	62	11.50	80	4.64
Municipal	418	7.27	53	9.83	76	4.41
Corporate	1,045	18.20	101	18.74	837	48.52
Foreign Bonds	18	.32	83	15.40	20	1.16
Total Bonds	2,310	40.22	339	62.89	1,227	71.13
Canadian Stocks						
Preferred	15	.26	6	1.11	2	.11
Common	95	1.66	58	10.76	-	
Foreign Stocks						
Preferred	-	-	-	-	-	-
Common	70	1.22	-	-	-	-
Total Stocks	180	3.14	.64	11.87	2	.11
Mortgage Loans**	2,536	44.17	104	19.30	370	21.45
Real Estate	265	4.62	13	2.41	7	.41
Policy Loans	260	4.53	10	1.86	74	4.29
Cash	30	.52	2	.37	17	.99
Total Invested Assets	5.581	97.20	532	98.70	1,697	98.38
Other Assets	161***	2.80	7	1.30	28	1.62
Total Assets	5,742	100.00	539	100.00	1,725	100.00

* Canadian companies' assets are shown at book values, non-resident companies' assets at market values. Market values for Canadian companies' stocks are about double book values.

** Includes agreements of sale.

*** Includes the mutualizing companies' holdings of their own shares in the amount of $ 48.6 million.

5.62 United States life insurance companies had an additional $2.4 billion invested in Canada on behalf of United States policyholders. These investments are shown in Table 5.g.

Table 5.g

Non-Trusted Canadian Investments of United States Life Insurance Companies - End of 1960

	(000,000)
Government of Canada bonds	$ 100
Provincial bonds	370
Municipal bonds	470
Corporate bonds	1,160
Mortgage loans	300
	$2,400

Investment in Financial Intermediaries

5.63 The debt obligations and shares of other financial intermediaries provide an acceptable avenue of investment. Indeed, if it were not for the shares of the chartered banks the volume of investment-grade common stocks in Canada would be greatly reduced.

5.64 A survey of the 20 life insurance companies with the largest asset holdings in Canada was undertaken to determine their investment in other financial intermediaries. These other financial intermediaries were taken to include chartered banks, investment trusts, mutual funds, finance companies, credit societies and trust and loan companies.

5.65 The investment in bonds issued in Canada of such intermediaries by these 20 life insurance companies

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Non-Trusteed Canadian Investments of United States Life Insurance Companies - End of 1960

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Investment in Financial Intermediaries

5.63 The debt obligations and shares of other financial intermediaries provide an acceptable avenue of investment. Indeed, if it were not for the shares of the chartered banks the volume of investment-grade common stocks in Canada would be greatly reduced.

5.64 A survey of the 20 life insurance companies with the largest asset holdings in Canada was undertaken to determine their investment in other financial intermediaries. These other financial intermediaries were taken to include chartered banks, investment trusts, mutual funds, finance companies, credit societies and trust and loan companies.

5.65 The investment in bonds issued in Canada of such intermediaries by these 20 life insurance companies

amounted to $278 million or less than 4 per cent of their assets. The book value of the common and preferred stocks of financial intermediaries held by the same companies amounted to $38 million, while the market value of these securities was about twice as large. In any case, since the market value of outstanding Canadian bank stocks alone at the end of 1961 amounted to nearly $2 billion, it is evident that the share interest of life insurance companies in this field is relatively insignificant.

The "Voting" of Common Stock

5.66 Canadian life insurance companies seldom send a representative to shareholders' meetings of companies in which they have a common stock investment. In supervising their investments, however, some life insurance company investment officers may meet with the management of the companies in whose shares they have investments in order to ascertain company pgoress and prospects.

5.67 Most life companies follow the practice of "voting" their shares by proxy. It is usual for shares to be "voted" as requested by management. A survey of 17 of the largest life companies operating in Canada disclosed that during 1961 nearly 800 proxies for "voting" of common shares in Canadian corporations were received from the managements of those corporations and that 93 per cent were "voted" as requested and 7 per cent were not "voted".

5.68 Canadian federally-registered life companies

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are forbidden by law from acquiring more than 30 per cent of the common stock of any one corporation. In the case of non-resident companies, this limitation applies only to assets vested in trust in Canada. Holdings by individual life companies usually constitute only a small percentage of a corporation's total stock. In only three cases did any one of the 17 life insurance companies surveyed hold more than 10 per cent of any corporation's stock outstanding at the end of 1961. The life insurance companies do not attempt to use their common stock holdings to exert influence over the management of other companies.

A COMPARISON OF THE INVESTMENT PRACTICES OF BRITISH, CANADIAN AND UNITED STATES LIFE INSURANCE COMPANIES

5.69 Marked differences of emphasis in certain categories of investment are evident from Table 5.h which compares the portfolios of British, Canadian and United States life insurance companies.

Table 5.h

World-wide Life Insurance Portfolios*
of British, Canadian and United States Companies

	1959			1960		
	Brit.	Can.	U.S.	Brit.	Can.	U.S.
Bonds & Preferred Stocks	46.6	51.1	53.6	44.8	50.1	52.8
Common Stocks	20.6	3.7	2.7	21.9	3.8	2.8
Mortgages	15.4	36.8	36.1	16.0	37.5	36.5
Real Estate	10.0	3.4	3.4	10.1	3.4	3.3
Other Invested Assets	7.4	5.0	4.2	7.2	5.2	4.6

Sources: Britain - Reports of members of the British Insurance Association with Head Office in the United Kingdom.

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Real Estate	10.0	3.4	3.4	10.1	3.4	3.3
Other Invested Assets	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Sources: Britain - Reports of members of the British Insurance Association with Head Office in the United Kingdom.

Canada - Annual Reports of the Superintendent of Insurance for Canada.

United States
- Life Insurance Association of America.

* The valuation bases used in the three countries are not strictly comparable.

5.70 In each case bonds (including guaranteed or preferred stocks) account for approximately half of total invested assets. This recognizes the fact that life insurance policies contain built-in guarantees of capital and interest which require assets involving fixed income and a guarantee of capital.

5.71 Mortgages which are also regarded as suitable for life insurance investments amount on the average to nearly 37 per cent of the assets of the Canadian and United States companies, but to only 15 per cent or 16 per cent of the British companies' assets. The reason for this would appear to be that the yield obtainable on mortgages in the United Kingdom is relatively less attractive. This has had the result of forcing insurance funds into equities and real estate where past experience indicates that great yields may be expected over the long term. In Great Britain also there is keen competition for mortgage business from the building societies which have no counterpart in Canada. These societies accept interest-bearing deposits which come largely from small investors and they invest these funds mainly in residential mortgages. The interest payable on the deposits and the mortgage interest are both subject to change at short notice and the result is to associate the yield on this type of mortgage investment with that of short-term

funds rather than to the long-term yield.

5.72 In Canada and in the United States, the yield on mortgages is traditionally associated with that on long-term bonds after allowance for the higher rate of investment expense. Government-insured and guaranteed mortgages in both countries have also accounted for a large volume of mortgage investment by the life insurance companies.

5.73 Real estate forms a small part of the portfolio of the Canadian and United States companies, but, in Great Britain, there has recently been a move by the larger companies in association with development companies to channel funds into real estate in the expectation that through the improvement and development of a site, a long-term high yielding investment will be created.

5.74 It is in common stock investment however that the main difference between British and Canadian or United States companies is apparent. The reason for the difference is discussed under three headings.

<u>Legislation and Supervision by Government</u>

5.75 In Great Britain there is an almost complete lack of restriction on the powers of investment. The only stipulation as regards the values at which assets appear in the balance sheet is that the balance sheet must state how the values of stock exchange securities are arrived at, and a certificate must be appended to the effect that the assets are in the aggregate dully of the value stated less any investment reserve fund. In practice stock exchange securities are usually valued in the aggregate at an amount not greater than their total

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market value and non-stock exchange securities are valued at cost. On the liabilities side, within the area of accepted actuarial principles the actuary of a company has freedom to fix, or vary from time to time, the interest rate basis of accumulation for the actuarial reserves. A fall in asset values resulting from higher market yields can be compensated for by applying higher interest rates to the basis for valuing the liabilities if the actuary so decides.

5.76 In Canada and the United States, on the other hand, strict supervision and legislative restriction in matters affecting investment powers and valuation of assets and liabilities. There is an upper limit to the amounts which may be invested in equities and there are qualitative tests for the eligibility of different stocks as investments. Valuation of market prices is required for most stock exchange securities, including common stocks, and minimum bases for the valuation of liabilities are laid down. Moreover - and this is a particularly important restrictive force - even within the scope of the statutory bases of valuation, there is little freedom to vary the basis for calculating actuarial reserves since guaranteed cash values are linked with the amounts of these reserves.

5.77 Market values of common stocks are subject to fairly wide fluctuations and within a rigid framework of restriction, prudence alone must induce a Canadian or United States company to limit its common stock investment so that a fall in market values will not seriously affect its surplus position.

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Variation in Nature of Insurance Contracts

5.78 In the United Kingdom, because of the income tax relief allowed on life insurance premiums, the emphasis tends to be laid on endowment contracts rather than on whole life contracts. On both sides of the Atlantic there is a growing trend to term insurance, but this is more marked on the North American continent than it is, as yet, in the United Kingdom. Again, in the United Kingdom the amount of pension and annuity business transacted by insurance companies is possibly greater than in Canada and the United States where trust and other companies are particularly active in this field. As a result, in Great Britain there is a greater concentration on the savings element and less on the protective element in insurance contracts than is found in Canada and the United States. This has contributed to a greater preference for longer-term investments including common stocks.

5.79 The practice of declaring dividends in the form of reversionary additions to the sum assured, which is almost universal in the United Kingdom, also lends itself to the concept of long-term investment accumulation and the reserves built up for future bonus declarations may form a cushion against a temporary recession in market values.

5.80 It may also be noted that guaranteed cash values are not universally available in the United Kingdom and that policy holders' recourse to the cash values of policies is almost certainly much less than it is in North America. There is therefore a lesser

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need for liquidity - or at least "marketability" - among the British companies.

Market Conditions

5.81 Both in the United Kingdom and United States, there is a wide market for equity stocks and, subject to the conditions and differences mentioned above, many life insurance companies in the United Kingdom and the United States are active purchasers in their respective markets. In addition, many Canadian companies are active purchasers in both markets.

5.82 However, the market in Canada for investment-grade shares is narrow. Many important Canadian companies are wholly-owned subsidiaries of non-resident corporations and there is a high degree of government ownership of utilities. Purchases by individuals, who have the benefit of the 20 per cent income tax credit, and by investment trusts - in both cases with investment objectives different from those of insurance companies - also tend to increase the price level and make these stocks less attractive to the insurance companies.

5.83 It would be wrong, of course, to deduce from this that life insurance companies are not active in the Canadian stock market. Some of the British companies doing business here are active purchasers up to the limits allowed by law. Some Canadian companies have been increasing their holdings. The new power to accumulate equities in segregated funds will doubtless contribute to increasing purchases of Canadian common stocks by the life insurance companies in Canada.

THE ORGANIZATION OF THE INVESTMENT FUNCTION

5.84 The directors of a life insurance company are responsible for the administration of their company and for compliance with the insurance laws. They determine its general policy and appoint officers to conduct day-to-day operations and to give effect to the policies which they have laid down.

5.85 Directors are persons with wide business experience and sound judgment on whom policyholders and shareholders know they can rely to discharge their responsibilities. Most life insurance company directors are also directors of companies in other lines of business. In this way the widest possible knowledge and the ablest judgment are brought to the management of the individual companies in the service of their policyholders.

5.86 There is a considerable variation in the organization of the investment function of life insurance companies operating in Canada. Differences in the organization of the investment operation are partly dependent upon company size and whether the company is Canadian or has a head office abroad.

5.87 The board of directors, of course, carries the fundamental responsibility for all investment decisions. It reviews the general investment policy of the company, approves investment transactions, and grants authorities to facilitate the operation of the investment department. It usually establishes one or more investment or finance committees. These committees are often composed of board members with special knowledge

of investment matters and sometimes include the senior investment officer of the company who may himself be a director. Investment committees meet frequently and are responsible for formulating a company's investment policy. Before larger investment transactions are made, they usually must be approved by the investment committee.

5.88 Most companies have a senior officer, usually a vice-president, in charge of their investment operation. Some companies, however, favour the splitting of responsibility between two or more senior investment officers, each officer having responsibility for a certain area of operation, such as one for mortgage investments and one for security investments. Depending upon the size of the company there are often several investment officers, each in charge of a particular area or group of investments, reporting to the senior investment officer or officers.

5.89 Canadian security investments are managed from the head offices of the companies. Mortgage investments are supervised from head office but the larger companies usually also have mortgage offices with local managers located across Canada.

5.90 It is in the area of the discretionary authority granted investment officers that there is probably the widest difference between companies. Some companies favour tight control with little independent authority given investment officers. Other companies, however, grant broad discretionary powers to their investment officers. Some mortgage branch managers are given no authority in the granting of loans without

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head office approval while other companies allow mortgage branch managers to make loans to a certain maximum on their own discretion.

5.91 Where an investment decision is taken depends upon its nature. Routine matters are often dealt with by the investment officers under authorities granted either by the boards or the investment committees. Non-routine matters and investments involving greater amounts of money often must proceed to an investment committee before action can be taken.

5.92 Some of the major non-Canadian companies operating here give considerable authority to their investment officers in Canada although major policy decisions and the approval of larger investments must often be made at head offices abroad. In the case of these companies, the Canadian investment departments are similar to those of Canadian companies and their operation often follows the same pattern.

5.93 Most companies place a high priority on the building and maintaining of highly skilled investment staff. In recent years the practice has been to recruit new personnel at the University level and to give new entrants a comprehensive course of training in investment work.

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SECTION 6

SOME VIEWS ON FISCAL AND MONETARY POLICY

OBJECTIVES OF ECONOMIC POLICY

6.1 There would seem to be fairly general agreement on the objectives of economic policy that should be sought by Canadians in fashioning their national policies. These objectives include:

(a) The maintenance of a high level of employment and income for the productive members of the community.

(b) The maintenance of reasonable price stability in the purchasing power of the dollar and defense of its external value.

(c) The promotion of a sustained and sustainable rate of growth within the economy.

(d) The provision of a basic floor and social welfare, as warranted by our ability to provide it, for the aged, widows and orphans, the permanently disabled and those temporarily unemployed.

6.2 It is generally agreed, too, that the fashioning of policies to these ends should take place within a society that recognizes the sovereignty of the individual and is organized so that the greatest possible freedom of choice - to work, to produce, to consume, to save and to progress - remains with the individual. Such a society derives real benefit from the initiative and self-reliance which it engenders amongst its citizens.

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6.3 It must be recognized, however, that the fashioning of policies to achieve these objectives must take into account Canada's reliance on foreign trade. Performance will rarely be perfect because of the somewhat unpredictable effect of external influences on the domestic economy and because of the difficulties of keeping the various aspects of different policies continuously co-ordinated and in balance. Nevertheless, government should continuously strive for the co-ordination and balance which are so essential.

6.4 The Association believes there is nothing inconsistent in these long-run objectives. It believes they are possible of attainment or virtual attainment if Canadians have the wisdom, through their elected representatives, to make well-balanced choices and sound decisions in public policy. Actions designed for either the stimulation or restriction of the economy in the short run will undoubtedly be necessary from time to time to keep progress toward our objectives in harmony and in balance.

NEED FOR UNIFIED FINANCIAL POLICIES

6.5 Although the Commission has asked specifically for our views on the appropriate role for monetary policy and its limitations, we find it extremely difficult to regard any particular facet of national policy in isolation. In the financial sense it is particularly difficult to dissociate monetary policy from fiscal policy, debt management policy and exchange policy. When co-ordinated each derives strength from the others.

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When not co-ordinated, no one policy, and particularly monetary policy, can make up, at least for long, for any shortcomings in other policies.

6.6 Monetary policy we would define as that part of financial policy which is concerned with the volume of the supply of money, the control of credit through the banking system and its reflection on the level of interest rates. The other three integral parts of financial policy are:

(a) Debt management polich which is concerned with the ownership, interest cost and maturity structure of the federal debt.

(b) Fiscal policy which is concerned with taxation levels and sources, with expenditures and with the effects of cash surpluses or deficits.

(c) Exchange policy which is concerned with the external value of our dollar.

6.7 It follows then that financial policy must be co-ordinated within itself and in turn financial policy must be co-ordinated with other economic and social policies.

6.8 One major problem is that although there is a great volume of theoretical studies available as guidance for those charged with the formulation and execution of financial policy, there is only a relatively modest amount of actual experience. It is about thirty years since governments generally abandoned the mechanical disciplines of the gold standard and adopted the much more permissive and flexible system of

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RESPONSIBILITY FOR MONETARY POLICY

6.9 The harmony and co-ordination to be desired in financial policy leads to the conclusion that government must accept ultimate responsibility for monetary policy just as it must for other parts of financial policy.

6.10 In saying this we stress the word "ultimate". The initiation and implementation of monetary policy should, in the first instance, be the responsibility of the management of the Bank of Canada and in the pursuit of its objectives in the monetary sphere it should be accorded wide latitude. The Association suggests that amendments to the Bank of Canada Act should make this abundantly clear.

6.11 If, at any time, the views of government and of the Governor differ on the appropriate monetary policy to be followed and such differences cannot be reconciled by discussion, then government views should be set forth in a directive to the Bank. If the Governor should then feel that such directive is not consistent with or compatible with the Bank's objectives under the Bank of Canada Act or with its own view of the developing situation, he should feel called upon to resign, thus

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bringing differences of view and the reasons therefor to public attention. Such a brake on any unwarranted or questionable alternation in the volume of credit is a necessary safeguard against the possible abuse of the machinery of credit creation for political ends.

ROLE OF MONETARY POLICY

6.12 There would appear to be two basic views as to the appropriate role for monetary policy. There are those who hold that the Bank of Canada should seek to carry out its monetary policy by varying the money supply, changing interest rate levels and influencing liquidity. This we would term the quantitative approach. There are others who feel that the Bank of Canada should be concerned directly with the allocation of resources and should attempt not only to determine the amount of credit but also how it is to be used. This we would term the qualitative approach. The Association subscribes to the former view, that is, the quantitative approach and to the extent that the operations of the capital market lead to distortion or result in an uneven or undesirable flow of funds to ultimate users, correctives should be applied by government rather than constituting them as the continuing task of the central bank.

6.13 Monetary policy thus becomes essentially the provision of a volume of money and credit adequate for the developing situation with due regard for the Bank's objectives. Monetary policy, then, working through a responsive capital market and responsive financial intermediaries, can seek through the effect

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of its operations on the levels of liquidity and interest rates to augment or dampen the rate of economic growth, to contribute to price stability and act as a balance wheel in regulating economic pgoress.

6.14 An important limitation on domestically initiated changes in interest rate levels is the impact such changes may have on international capital flows. Whether we like it or not, the Canadian financial market is oriented toward that of the United States, and Canadian monetary policy can be effective only within limits established in that market. Admittedly these limits may not be too restrictive because of parallel business cycles but any dissimilar monetary policy can lead to large-scale movements of short-term money. A "free" dollar or "floating" dollar offers some cushion that any given monetary policy will not be abortive or distorted but even variations in the exchange rate have desirable limitations. The recent move to "fix" the exchange rate of the Canadian dollar throws the weight of the adjustment on the reserves of the Exchange Fund and whatever help is forthcoming from the International Monetary Fund or external borrowings.

6.15 Although monetary policy is a flexible instrument, it is still general in its application and can never be a substitute, at least for long, for deficiencies in other financial, economic or social policies. In other words, it can never be an automatic cure-all for all the economic problems that confront the country or regions of the country from time to time. At best it can only hope to hold the fort temporarily,

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5.15 Although monetary policy is a flexible instrument, it is still general in its application and can never be a substitute, at least for long, for deficiencies in other financial, economic or social policies. In other words, it can never be an automatic cure-all for all the economic problems that confront the country or regions of the country from time to time. [illegible] It can only hope to hold the fort temporarily,

pending more basic changes in other policies designed to meet the problems and then assist during the period of transition.

6.16 Monetary policy must be continuously framed against the emerging situation. To the extent that all aspects of financial policy are co-ordinated, the initiation and implementation of monetary policy is made easier. To the extent that co-ordination does not take place, monetary policy itself can be warped by new government cash requirements for deficit financing, by refinancing or debt conversion or by the change in exchange reserves resulting from external pressures on the dollar. The result is that changes in money supply can be greater than would be desirable for monetary or economic reasons alone.

6.17 Monetary policy to be effective must also operate against a background of confidence - confidence in government policy in all its aspects as well as confidence in reasonable stability in the level of prices. Lack of confidence in financial policy is quickly felt in the financial markets and can stulify the best efforts of monetary management by making the market unresponsive to the changes in liquidity or interest rate levels which might normally be expected to flow from alterations in the volume of money.

6.18 We have indicated that monetary policy should work through a responsive capital market and responsive financial intermediaries. Generally, we would subscribe to the view that the responsiveness of a capital market is enhanced by having as few barriers as possible to the

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free flow of funds through it, thus imparting a high degree of fluidity to the money flow and allowing a high degree of liquidity to the financial obligations.

6.19 Responsive financial intermediaries we would classify as those whose activities within their own frame of reference tend to follow and amplify monetary policy as it expresses itself through the levels of interest rates and the degree of liquidity.

6.20 Monetary plicy is made effective, in the main, by the Bank of Canada through its so-called "open market operations", that is, its buying and selling of securities. In so doing, it varies the size of the deposits which the chartered banks must maintain with it and thus varies the total of chartered bank assets. An increase in these deposits allows an increase in chartered bank activities, while a decrease means a reduction in the moneys they have available.

6.21 Variations of this kind (because of the 8 per cent reserve requirement) affect directly the availability of chartered bank commercial and other loans and their funds for security investment. Chartered bank activities in the lending field are always subject to competition from other lenders. In periods of restriction, however, they bear the brunt of monetary action in the first instance. Inability to lend immediately sends potential borrowers searching for alternative sources of credit. To the extent that such borrowers can obtain their requirements within the capital market by alternative methods of financing, the full effect of monetary policy is merely delayed -- a

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factor which the monetary authorities must take into account. If immediate control of any particular allocation of funds is deemed necessary, it would seem preferable to attack the problem directly through temporary fiscal regulations or directives rather than attempt to bring other financial intermediaries under some form of continuing relationship with the central bank.

EXTENSION OF DIRECT CONTROLS

6.22 The Association believes however that in peace-time at least, there is rarely a case for the extension of direct controls throughout the economy, unless there is a clear case of speculative or other excesses which are leading to an imprudent use of resources and which are clearly not in the public interest. If and when such a situation exists in a form not susceptible to control through the normal operations of monetary policy and the capital market, then such correctives should emanate from the Minister of Finance.

6.23 Direct controls of this character actually mean the allocation by government of the credit resources of the economy and substitute its judgment for the judgment of the many who participate in the capital market. Excesses of the type that need to be controlled by this means are invariably only symptoms of a deep-seated maladjustment. The direct control may alleviate the symptom but do nothing to cure the disease, and it is the disease that is important.

6.24 Direct controls also require detailed regulations and enforcement officers to curb pressures and evasions.

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They are malignant in character. They tend to grow on themselves - to plug loopholes and to provide for a myriad of special situations. In our view, direct controls of this nature should be used only as a last resort. They are no substitute under normal circumstances for the judgment and discipline of the market-place and in abnormal circumstances direct controls are only a palliative, not a cure.

EXTENSION OF CONTROLS FOR THE PURPOSE OF ALLOCATING SAVINGS

6.25 Difficulties which may be experienced from time to time by certain potential borrowers or classes of borrower in obtaining funds through the capital market at what they may consider to be reasonable interest rates usually lead to suggestions that governmental authorities should impose, by legislation or otherwise, restrictions whereby financial intermediaries are required to invest a certain proportion of their funds in certain categories of investment. Such suggestions usually arise on behalf of a "social need" that is said to exist, such as that contained in housing finance and municipal loans or on behalf of a credit gap within the private sector, such as loans to small business and venture capital.

6.26 It is probably a truism that there is never a time when all borrowing "needs" can be met from the accrued and accruing savings of the nation. Under such circumstances, some method of establishing priorities must exist. This is one of the basic functions of the capital market where borrowers and lenders meet. Such

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a method may have its imperfections, but it has never been established that the substitution of government direction for the multitude of decisions in the market-place would result in the establishment of more effective allocation.

6.27 If such restrictions or directions by government to financial intermediaries were to take the form of requiring, say, certain minimum amounts to be invested in any specific category of assets, government in effect guarantees to borrowers within that category a volume of funds for their purposes. To this extent at least, such borrowers and their needs are removed from examination in the market-place.

6.28 The funds, for example, which the life insurance companies have to invest are the voluntary savings of some nine million policyholders. The framework of rules and regulations to which they are subject in the insurance Acts has as its aim the safety of the investment or the limitation of economic power. Within this framework, the life insurance companies are free to maximize their investment return (with due regard for safety, of course) for their policyholders. The analysis of their assets shows the wide diversification of investment both by category and by region achieved by the companies.

6.29 The life insurance companies can only invest the funds they are able to attract. Any regulation as to the minimum proportion of assets that must be placed in any one or more categories must reduce the amount of funds that can be made available for other

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PUBLIC UNDERSTANDING DESIRABLE

6.30 Confidence in financial policy including monetary policy is enhanced by public understanding and general agreement with its objectives and methods of achievement.

6.31 Fuller public understanding of the role of monetary policy itself is desirable but statements by the Bank of Canada should be confined as far as possible to the considerations involved in monetary policy and its implementation. It should give the fullest possible explanation of what it has done. The Bank should publish both monthly and weekly statistics and explanatory notes concerning the financial markets - the money supply, the condition of the chartered banks, an analysis of their general loans, the level of interest rates, the state of the federal debt and so on. Every effort should be made to make these as exhaustive as possible and to publish at the earliest moment. The Annual Report of the Governor, which is required to be transmitted to the

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Minister of Finance, should contain an analysis of the Bank's operations in the context of the economy generally.

6.32 The Bank's developing views and its intent should be constantly before its responsible Minister but public statements as to its intentions should only come at rare intervals, for example, when some change in operating procedure or some major change in policy direction is imminent. Other than this, it would seem to us that the Bank of Canada should be able to pursue its objectives in reasonable anonymity.

6.33 This is not to say that the central bank should always remain silent. Its right to be heard in the pursuit of its objectives should be respected and its duty to dissent under appropriate circumstances recognized.

DISCUSSION AND PERSUASION

?./$ One further method of promoting understanding of financial and monetary policy and assisting in its implementation is by private discussion by central bank management with interested groups. Discussions of this character with the chartered banks take place, we believe, at fairly regular intervals. Discussions with the money market dealers and others of the financial community undoubtedly occur from time to time. Some of these are initiated by the Bank itself and some by the interested groups. Discussions of this sort and a free exchange of views cannot help but be constructive and build the confidence of each in the other.

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course, there were several discussions regarding foreign exchange control and war finance; the latter helped to funnel into war loans virtually all the accruing cash resources of the companies. In March 1951 the Association's Special Committee on Inflation met with officials of the Bank of Canada. This was at the Special Committee's request. Discussion included the subject of the companies' investment in federal government bonds. Early in 1952 an arrangement was concluded with the then Governor for a monthly reporting of the Canadian investment transactions of twelve large companies. These began to be published in the Bank's Statistical Summary about three years later and have continued since. In 1958 there was a direct approach by the Minister of Finance to many of the companies as well as other representatives from the financial community in advance of the Conversion Loan.

6.36 These meetings and discussions were an effective means of communication and we believe useful at the time and in the context of events. In our opinion, they should continue to be contemplated when matters of importance arise. We believe, however, that they are most effective when conducted without any undue publicity.

RE-DISCOUNT RATE

6.37 The Association finds it difficult to believe that there is any great matter of principle involved in the prolonged public discussion concerning the relative merits of the "floating" re-discount and the

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6.37 The Association finds it difficult to believe that there is any great matter of principle involved in the prolonged public discussion concerning the relative merits of the "floating" re-discount and the

"stated" re-discount rate. Rather we would feel the method of setting the re-discount rate is basically an operating procedure and as such, whatever is decided upon, it should be placed in the position of being satisfactory to the central bank, to the chartered banks and to the financial community generally and thus removed from the area of contention. To the extent that changes in the re-discount rate can be made meaningful in terms of signalling changes in the direction of monetary policy, so much the better.

PRICE STABILITY

6.38 For well over 100 years life insurance companies have been performing services of steadily increasing value for their policyholders and for the country. Consequently, they have had and continue to have an interest in all our national objectives and in our progress toward their achievement.

6.39 On behalf of their policyholders they have a particular interest in the maintenance of reasonable price stability. Life insurance contracts, whether owned basically for their protection features or for their accumulated savings values, are long-term contracts. Many years may elapse between the time of payment of the first premium and the payment of the last benefit. Thus maintenance of price stability or the avoidance of inflation is of prime importance to policyholders in the safeguarding of the values of their policies and the companies' control of operating costs on behalf of policyholders.

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6.40 Inflation is always a threat. The rise of prices following World War II has been of sufficiently recent experience and of sufficient magnitude to make everyone aware of its dangers and should strengthen our determination to avoid its repetition. The life insurance industry has made its views known on the importance of this subject on several occasions in recent years. The Association believes that it is highly important that the nation manage its affairs in such a way as to stop the almost continuous upward drift in the price level.

6.41 Concern about long-term stability in prices is not confined to the life insurance companies. Knowledge of economic phenomena is becoming more widespread. Greater numbers of citizens understand that inflation can wipe out their savings, wherever they are, just as effectively as prolonged unemployment. They understand that difficulties are created for many salaried workers and for all those living on pensions or on income from fixed-interest securities. They understand that rising prices reduce Canada's ability to sell in foreign markets which affects her export industries adversely.

6.42 The problem of inflation arises from an imbalance in economic affairs. Although it manifests itself as a monetary phenomenon in the sense of rising prices, its roots lie much deeper in the stream of economic activity and in the continuing maze of decisions made by citizens as individuals, as corporations and as governments. No ready cure is available. Just as causes are complex, so the problem of cure likewise is complex. Just as the causes may differ from time to

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to time, so the attack at the problem may have varied emphasis. One thing is certain - just as combatting recession requires the use of a broad arsenal of weapons, so the combatting of inflation requires an equally broad attack, not only on the monetary front but also in fiscal matters and in economic policy generally as well as in individual and corporation affairs.

6.43 The first prerequisite is a desire - indeed a determination - on the part of government to place reasonable price stability along with a high level of employment and income as the two major objectives of public policy.

6.44 The second prerequisite should be a willingness to use all the paths which will advance the economy toward the goal of reasonable price stability - whether they be monetary or fiscal. Policies of restraint cannot be expected to be as popular as policies for reducing unemployment but from time to time as the economy ebbs and flows, will become equally necessary. Monetary policy which will always be in the forefront of restraint can never be sufficient of itself. Monetary policy at these times needs powerful support from fiscal policy.

6.45 The necessity of laying continuing stress on price stability is underlined by the reliance which must be placed in the economy on satisfactory and continuing debtor-creditor relationships, and on the continuous process of saving and debt formation. This requires the prior accumulation of savings on the one hand and their transfer through debt instruments to others.

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Government borrowings at all levels must take place through debt instruments. Most corporate and individual borrowing is in fixed-dollar form. Any circumstances, such as inflation, which destroys confidence in the long-term purchasing power of the dollar will reduce savings, impede capital formation, place emphasis on liquidity, promote speculation and imperil the future sound growth of the economy.

OLD AGE SECURITY

6.46 Certain aspects of fiscal policy, which reflect social policy, that could have their effect on the life insurance business are a compulsory medical care plan and an additional old age pension plan. Both will have an effect on the balance of government revenues and expenditures and the latter a particular effect on the capital market.

6.47 For example, the Old Age Security plan was established in 1952 with the support of all political parties and of many other interested groups, including the life insurance companies. It was designed to provide everyone with a basic income at age 70 - a floor on which the individual could build his own retirement program.

6.48 Canadians have shown their willingness to do this. Since 1952, membership in private pension plans has increased from 1¼ million to 2 million employees. More than three-quarters of all those engaged in industry are employed in establishments having pension plans. The growth of other private savings has also been vigorous.

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6.49 The present Old Age Security plan has many advantages. Because of its universal nature - $65 a month to everyone - the plan helps most the low earner whose need is greatest. It is simple and inexpensive to administer and ensures the payment of the maximum benefit for each tax dollar collected for this purpose.

6.50 Since the current plan was begun ten years ago, the benefit has been increased on three on three occasions - from $40 to $65 - and has more than kept pace with increasing living costs. Changes in benefit are immediately reflected in payments to the recipients.

6.51 The operation of the plan has sharply reduced the proportion of Canadians over 70 who receive needs-tested assistance. This proportion is now 10 per cent as compared with 46 per cent in 1951.

6.52 The present $65 monthly benefit is already more generous than the average pension under the United States Social Security system having regard to the lower income levels in Canada. Indeed, for married couples the Canadian benefit is relatively much larger because under the United States system married couples only receive 1½ times the single benefit.

6.53 The life insurance companies in Canada are concerned about the substantial commitments governments have already made in the welfare area. The expenditures involved are permanent and increasing. The proportion of national production used for these purposes has risen greatly in post-war years and additions to our present commitments cannot help but reduce the amounts available for other essential services.

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For these reasons we feel that Canada should not add a compulsory pension plan of any type to the present universal flat benefit plan.

6.55 Widespread interest in a pension plan of the United States Social Security type is evident. Many Canadians misunderstand that program and feel that the amount each person contributes comes back to him in later years as retirement income. Contributions are therefore not looked upon as taxes. In actual practice, however, no government plan of which we are aware, including the United States plan, equates an individual's benefits to his contributions. Even if a government-operated plan tried to do so, irresistible pressures would arise to borrow from the funds required for <u>future</u> benefit payments in order to make <u>current</u> payments.

6.56 Under the United States Social Security program, pensioners are currently receiving income payments the value of which far exceeds the value of their accumulated contributions - this "subsidy" amounts to as much as $22,000 in some individual cases. Furthermore, these "subsidies" at present are larger for pensioners who had high earnings than for those who had low earnings.

6.57 While the benefits and contributions under the United States plan may appear today to be very attractive, a heavy share of the plan's cost is being deferred to future generations of taxpayers. The contribution rates are scheduled for a 50 per cent increase by 1968. This increase is necessary to maintain the level of benefits <u>now</u> being paid. If this increase comes into

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effect with benefits at their present level many contributors and their employers may be paying more in the future for their pensions than they would have to pay for equivalent pensions through private plans. The solution to this dilemma might well be to increase the benefits under the government's plan and once again add heavy costs for future generations.

6.58 Because of its inherent weaknesses, we are opposed to the addition of a government-operated plan providing graduated benefits on top of the present universal Old Age Security plan.

6.59 There are, however, certain groups where a high proportion of members need assistance, for example:

(a) all persons unable to work because of permanent disability, and

(b) all widows with dependent children.

If additional expenditures are to be made in the field of social welfare, the life insurance companies feel that first priority should be given to such groups as these by extending to them the advantages of a program of flat, uniform, basic benefits as a matter of right.

6.60 As we have saidk we feel that no compulsory pension plan of any type should be added to the present universal plan. If, nevertheless, it is decided that one should be instituted we urge that it be administered entirely through existing facilities rather than by the government and that such a program should have the following features:

(a) A contributor should be forced to participate only up to a benefit level which

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(a) A contributor should be forced to

will make it unlikely that further government assistance will be necessary when he retires.

(b) Each contributor should receive the amount of benefit that can be purchased by his own and his employer's contributions - no more and no less. Any subsidies considered desirable as a welfare measure can be provided more satisfactorily by the present flat benefit plan and needs-tested supplements for two reasons. Firstly, it is extremely unlikely that any graduated benefit plan can be made to apply to everyone and most of the persons not covered will be among the least fortunate in the community. Secondly, in any government-operated graduated benefit plan it is likely that those with higher earnings will get the larger subsidies.

6.61 A plan with the characteristics we feel are desirable could be implemented by requiring employed groups to establish "portable" pension benefits of at least a certain level but the groups should be free to select the type of private pension plan best suited to their needs. The life insurance companies, trust companies and other administrators of pension plans have demonstrated their ability to serve the public on an efficient and economical basis. The continued use of these existing facilities would avoid the weaknesses of a government-operated plan and in addition would have the following important advantages:

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contributor, to ensure payment of the benefits promised him. The interest earnings on these funds become substantial and help appreciably to pay for the benefits. This is in marked contrast to government-operated plans where contributions are paid out for current benefits and where, as a consequence, there is little saving and a correspondingly small interest income.

(b) The use of existing facilities would ensure the continued growth of the pension assets in private plans. The investment of these assets is a powerful factor in financing Canada's growing economy, helping to create job opportunities and developing our natural resources, our industrial capacity, our housing and our municipal and other services.

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SECTION 7

SOME VIEWS ON THE CAPITAL MARKET

7.1 Progress toward a country's economic objectives in a society like ours is both dependent on and facilitated by a well-developed capital market. Such a market grows as a country matures and, indeed, the degree of development of such a market can almost be said to be an indication of that country's maturity.

7.2 A well-developed capital market should be one that can provide a fairly continuous volume of trading in the different categories of financial obligations with their differing credit-worthiness and varying maturities. It should exhibit a high degree of sensitivity not only to the yields obtainable on these obligations but also to the relative yields as between the different obligations. This sensitivity should result from the factors of supply and demand as they exist from time to time or as they are made to exist through monetary influence. Such a market should also contain as few barriers or hindrances as possible to the free flow of funds throughout it, thus allowing the greatest freedom for interest rates to reflect the changing pressures of supply and demand.

7.3 The capital market in Canada has been growing and is becoming more fully developed over the years. Many deficiencies have been progressively overcome. For example, mention can be made of the growth of a short-term money market in the last seven years. The volume of government and corporate bond financing is further evidence of the market's development as is the volume

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of shares traded on our stock exchanges.

7.4 The capital market in Canada, however, has not reached full development yet by any means. Certain categories of financial assets, such as mortgages for example, have so far attained a lesser degree of liquidity in Canada than in some other countries and yields on such assets are not as responsive as they will undoubtedly become with further growth. Development of a capital market is, basically, an evolutionary process.

7.5 The Association feels, however, that the Canadian capital market today under normal circumstances is reasonably responsive to changing supply-demand relationships. Normal circumstances, of course, assume circumstances which do not exhibit any untoward fear of inflation on the one hand or any untoward fear of recession and deterioration of credit-worthiness on the other. Both of these conditions produce distortions. The Association also feels that the capital market is sufficiently broad, sufficiently flexible and sufficiently cohesive to allow a monetary policy to be reasonably effective.

7.6 That is not to say that further development cannot take place. There are, in the Association's view, certain improvements in procedure that might prove beneficial and certain areas where access to the capital market might be improved. It offers the following comments and observations for the Commission's consideration.

THE BOND MARKET

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7.8 Since the war, too, the size and scope of the market for provincial bonds has increased significantly. At present many outstanding provincial or provincial-guaranteed issues trade in sufficient volume and frequency to allow fairly firm and up-to-date quotations for reasonable size to be given at any time. Unlike the market in federal government bonds, however, the provincial market, as with the corporate and municipal bond markets, is conducted primarily through the investment dealers with investors.

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corporate bond issues and the relative infrequency with which many corporations finance their expansion through the capital market. Under such conditions quotations cannot be regularly made and often can only be obtained when specific purchase or sale is proposed. This is particularly true, as well, of the market for all but the larger municipal bond issues. This is only to be expected. Continued growth of the economy will undoutedly result in a still broader capital market and with increased public financing by corporations and municipalities, a more active market in these issues will follow.

7.10 With particular reference to new bond issues, a prime objective of the investment dealer should be to ensure prompt and full distribution. Institutional demand today constitutes a large percentage of effective demand for many bond issues and from time to time many life insurance companies have difficulty in obtaining from the dealers or syndicates as large a participation as they might wish in the first instance. They suggest that some consideration be given to the provision of information of the details of a new issue and of the borrower further in advance of the offering date and, after offering, they feel a prompt delivery date would assist in early and complete distribution.

7.11 The life insurance companies, traditionally, have been substantial buyers of municipal bonds. The fact that many municipalities are small and not too well known creates difficulties however. The pooling of municipal borrowing has been a fairly recent phenomenon.

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This has occurred naturally as metropolitan area governments have been created. It has occured naturally also as school districts and other joint projects have been expanded to include several municipalities. The Alberta Municipal Finance Corporation which with the provincial guarantee borrows for reloaning to the municipalities is another example. British Columbia also makes extensive use of the provincial guarantee. To the extent that municipal governments cannot borrow directly either because of lack of size or lack of credit-worthiness, it is suggested that some form of provincial sponsorship is the only effective way of adding the additional credit to allow access to the capital market. Care must be exercised, however, that such sponsorship through the provision of easier credit does not lead to the accumulation of municipal debts which will prove too burdensome to repay.

THE STOCK MARKET

7.12 The life insurance companies have found the facilities for trading in stocks through the members of the stock exchanges in Canada to be quite adequate, although the size of the market in investment-grade shares is not nearly as great as might be desired. There are about 310 Canadian common stocks that specifically qualify for investment under the Insurance Acts. Of this number about 200 are either so closely held or so seldom traded for various reasons that for practical purposes the effective number of available issues is reduced to just over 100.

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7.13 The growth and development of Canadian industry through the post-war period has opened up various new avenues of investment in common stocks. The petroleum and natural gas industries are two examples of such investment avenues. The further development of manufacturing and service industries should increase the number of quality-grade Canadian equities which institutional investors may find attractive. From this point of view it is unfortunate that so much of Canadian industry is foreign-owned and so many utility and transportation companies have had their shares paid off as they have been converted to government ownership. Another difficulty is that large proportions of the relatively narrow list of stocks of investment grade that are available tend to be put away in investment portfolios, thus reducing the prevailing supply still further.

7.14 The larger companies in the Association's membership again find some difficulty from time to time in dealing in large blocks (namely, multiple board lots). This is essentially a matter of size and may disappear if both the number and volume of shares of investment-grade equity issues expands.

7.15 To the life insurance companies investment-grade common stocks are those which either have or will shortly have a seven-year dividend history as required by the Insurance Acts. This can in no way be termed venture capital. Small new and high-risk companies have difficulty in raising both debt and equity capital. The Industrial Development Bank in recent years has

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supplied many such firms with financing mostly with debt capital although it is understood that some participation in equity has been taken.

7.16 The financing of new business today requires an amount of money that few investors care to place on one risk. A practical method of accomplishing the purpose, however, might be the formation of a development corporation which would be in turn financed by a large group of investors. This represents one method of obtaining a spread of risk through group participation that would be impossible of attainment by any one investor. Such a development corporation would be able to provide many small firms with both debt and equity capital and even assist in the provision of counsel. This would make a constructive contribution. Such development corporations would assist in the future growth of Canadian secondary manufacturing and service industry.

THE MORTGAGE MARKET

7.17 The mortgage market in Canada is effective in the sense of bringing lenders and borrowers together but as yet cannot be said to impart any real degree of liquidity to mortgage investments. As a consequence, changes in mortgage interest rates both conventional and N.H.A. tend to lag behind changes in interest rates of more highly liquid investments. Nevertheless, the monthly payments which characterize most mortgages today have in fact greatly enhanced the liquidity of this type of investment, to which the large annual flow of regular repayments attests.

[illegible]

unions, pension funds, endowment funds and estates - as well as individuals. The life insurance companies normally originate their loans either directly or through mortgage agents. They have been more or less permanent investors in this kind of debt obligation. They have set up the specialized facilities necessary for the administration of both residential and non-residential loans. For liquidity, however, they have relied on the process of regular repayments.

7.19 The federal government became particularly interested in the financing of new housing in 1935 when there appeared to be not only a reluctance to provide mortgage credit but also difficulty in financing the equity over and above the normal first mortgage of 60 per cent of value. The government also hoped to reactiv- the house construction industry and increase capital investment. At that time a basis of joint loans was worked out which allowed loans to 80 per cent of value with the government supplying 25 per cent of the loan. Interest rates were fixed by government and provision made for the sharing of losses. In 1954 this partnershi was superseded by a plan of mortgage insurance under the National Housing Act which plan, with some variations, has continued to the present time. At its inception the plan had the effect of reducing the contribution of government because all the money was advanced from

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the lending institutions. At the same time the chartered banks were empowered to make N.H.A. insured mortgage loans. Participation by the banks in this activity was virtually brought to a halt when the interest rate moved above the 6 per cent ceiling contained in the Bank Act. The existing sources of mortgage finance were augmented by government through direct loans and these funds of course came directly from the federal treasury.

7.20 The intervention of government in the financing of new housing in this fashion has assisted in the raising of the standards of housing, has promoted both the availability and uniformity of mortgage credit on a national basis and, through the reduction in down-payments and extension of the amortization period, has increased the number of those who can aspire to home ownership. On the other hand, the additional demands created by the government's emphasis on the need for new housing both for social reasons and for economic reasons associated with volume of capital investment have created other pressing financial needs, particularly at the municipal level. Housing programs of the magnitude desired have resulted in the creation of credit demands for the supply of new road, sewers, educational and shopping facilities and the other necessities of community living. Although the life insurance companies still remain the major source of private funds for mortgage finance, they also are a prime source of funds for municipalities and others to finance the varied ancillary and essential demands that are created with housing expansion.

7.21 The development of a secondary mortgage

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7.21 The development of a secondary mortgage

market which would broaden the band of investors interested in mortgages and increase the liquidity of mortgage investments would be desirable. A primary requisite of a secondary mortgage market is a method of assessing quality. Each mortgage investment has risks and hazards peculiar to itself. These result from factors affecting the property, its usefulness, its access to services and the credit-worthiness of the borrower. In practice it is almost necessary for an investor in the secondary market to actually inspect the real estate and the mortgage instrument itself. This procedure could prohibit a widespread and efficient secondary market operation as far as conventional loans are concerned.

7.22 N.H.A. mortgage insurance has gone a long way towards introducing greater uniformity of quality. It reduces the inherent risk factors to a minimum and thus makes each insured mortgage virtually as attractive as any other. However, even N.H.A. "insurance" does not guarantee a trouble-free investment. There is virtually no instance where the mortgage claim in event of trouble can be satisfied without loss to the lender where the "insurance" is relied on. For example, the claim for insurance is limited in point of time to a maximum of six months' interest at the mortgage rate and up to an additional twelve months at the mortgage rate less two. Since delivery of "vacant possession" is necessary, the time elapsing between the start of action to enforce security and the acquisition of title to the property is a hazard over which the mortgagee has little control.

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He can be subjected to retarding action by the borrower by subsequent encumbrances, by statutory delays designed to afford grace to the borrower and by delays in pursuing the action through the courts. Enactment of moratoria legislation can prevent the commencement and completion of mortgage actions and the effect of any debt adjustment legislation is not covered. Also, the insurance only partially covers the legal costs involved in acquiring title and possession. All these factors militate against imparting a high degree of liquidity to these mortgage instruments.

7.23 There have been a few sales of blocks of both conventional and insured mortgages from one insurance company to another by direct negotiation and a large number of sales of insured mortgages by banks to other buyers, chiefly pension funds. The successive sale of blocks of N.H.A. mortgages by Central Mortgage and Housing Corporation at auction is broadening the bank of investors and is helping to create the base from which a secondary mortgage market can develop.

7.24 In the United States there is a well developed "mortgage banking system ", the members of which act as originators and servicers for permanent investors in connection with Federal Housing Administration and Veterans' Administration insured loans. The existence of these specialists facilitates the sale of mortgages from one investor to another and increases liquidity in this form of investment. These packages of mortgages are bought and sold at par or at premiums and discounts thus providing yields to investors that vary from the

can be subjected to retarding action by the borrower by subsequent encumbrances, by statutory delays designed to afford grace to the borrower and by delays in pursuing the action through the courts. Enactment of moratoria legislation can prevent the commencement and completion of mortgage actions and the effect of any debt adjustment legislation is not covered. Also, the insurance only partially covers the legal costs involved in acquiring title and possession. All these factors militate against imparting a high degree of liquidity to these mortgage instruments.

7.23 There have been a few sales of blocks of both conventional and insured mortgages from one insurance company to another by direct negotiation and a large number of sales of insured mortgages by banks to other buyers, chiefly pension funds. The successive sale of blocks of N.H.A. mortgages by Central Mortgage and Housing Corporation at auction is broadening the bank of investors and is helping to create the base from which a secondary mortgage market can develop.

7.24 In the United States there is a well developed "mortgage banking system", the members of which act as originators and servicers for permanent investors in connection with Federal Housing Administration and Veterans' Administration insured loans. The existence of these specialists facilitates the sale of mortgages from one investor to another and increases liquidity in this form of investment. These packages of mortgages are bought and sold at par or at premiums and discounts providing yields to investors that vary from the

stated interest rate, similar to that which occurs in the bond market. This too creates a higher degree of responsiveness to changing interest rate levels.

7.25 The volume of mortgage credit in the housing fields forthcoming from sources of private savings will vary in relation to the condition of the housing market. Emphasis on residential construction for the sake of its contribution to the total of capital investment in the economy will undoubtedly lead to periods when supply outruns demand. In many areas today, for example, there would appear to be significant vacancy ratios and some unsold houses. Such periods of indigestion lead to a diminished supply of mortgage credit.

7.26 There have been suggestions over the years that N.H.A. mortgage insurance be made to apply to loans on existing houses. It is said that this would broaden the market for new houses and bring about a more economic use of existing space by allowing older occupants of larger houses to acquire other and smaller houses more in line with their reduced space requirements. It would also to some degree reduce the demand for second mortgage money with its large bonuses, high interest rates and other charges. On the other hand, the extension of N.H.A. insured loans to existing houses would not necessarily ensure that more new houses would be built. In fact, it could make less money available from private sources to finance new houses and thus might require more federal funds rather than less to maintain any desired volume of new house construction. Also, it would have the effect of monetizing or making liquid a large volume of past savings

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and appreciation in values from recent inflationary price rises and there is little or no guarantee that such savings would be directed into equity in other housing. Much of it could find its way into current expenditure and thus result in a large volume of dissaving. Further liberalization of mortgage terms on existing housing would likely operate to raise the price of those existing houses.

7.27 If such a course were to be adopted, in order to avoid abuses and to confine it to "housing" in the true sense of the word, it would be essential that the legislation limit the availability of the insured mortgage loan on existing houses to the bona fide purchaser of a single house who intends to reside in it. The lending value, too, must recognize fully the age of the house, its location, its physical condition and its remaining economic life. These factors should lead to the consideration of a maximum loan, of not more than 80 per cent, and to shorter amortization periods.

REAL ESTATE MARKET

7.28 The life insurance companies, while not large factors in the real estate market, believe that in Canada it is reasonably well developed through existing realtors and real estate boards. Acquisition and sale of real properties does not present any particular problems.

PARTICIPATION IN THE UNDERWRITING FIELD

7.29 The Association believes that the primary

role of the life insurance companies in the capital market is that of investors. That does not mean to say, however, that it may not be appropriate for them on occasion to extend into the field of underwriting securities jointly with investment dealers for subsequent distribution. In the British market, for example, the life insurance companies are active in this capacity.

DIRECT PLACEMENTS

7.30 Essentially, any financing which does not involve a public offering or distribution may be considered to be directly placed. This applies particularly to corporate debt issues which are sold through negotiation directly to one investor or a small group of investors in a non-public sale.

7.31 This method of placement has been more widely used in the United States than in Canada. A survey of 28 United States life insurance companies that account for 85 per cent of the corporate bond holdings of all United States life insurance companies shows that in each year since 1950 90 per cent of corporate bonds acquired have been by way of direct placements. At the end of 1960 74 per cent of corporate bonds held were classified as direct placements.

7.32 No corresponding data are available for Canada but it appears unlikely that anything more than one-third of life insurance companies' purchases of Canadian corporate bonds have been directly placed during the 1950's.

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7.33 One reason why the level of so-called direct

placements is so much higher in the United States stems from the effect of the Securities Act of 1933. The requirement of this Act that public issues be registered with all the attendant costs and delays involved in registration is a strong inducement to finance by way of direct sale. That direct sales have no reached similar proportions in Canada is no doubt due in part to fewer and less onerous regulations and in part to the fact that many of the Canadian life insurance companies appear to trade more extensively than their United States counterparts, thus affording some preference for public issues.

7.34 There are savings through direct placement in the cost of financing to the borrower, particularly in the case of smaller issues and smaller companies. There is also considerable flexibility in setting the terms of borrowing. Direct placements can be tailored to individual requirements and subsequently changed much more easily, if circumstances so require. Such issues often require much less time in negotiation. Statistical information is not made public and the take-down of funds can be arranged to conform more readily with the requirements of the borrower.

7.35 On the other hand, the directly placed issue definitely lacks marketability. As a result, the interest cost to the borrower may be somewhat higher and restrictive clauses somewhat stiffer. Also, from the borrower's point of view, if its financial statistics are already public knowledge, there is frequently some advantage in having its securities held by the public generally

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rather than by a few large investors.

FULLER FINANCIAL INFORMATION

7.36 Institutional investors, of course, are interested in obtaining on a regular and continuing basis the fullest financial information possible. Over the years such information concerning corporations has greatly improved but there is room for further improvement. The Association believes, however, that pressure of public opinion rather than legislation should be relied on in the main to effect this improvement.

7.37 The Association suggests, however, that it would be helpful if the chartered banks would release through the regular weekly Bank of Canada statement a breakdown of "general loans". As a minimum it is suggested that this breakdown should show separately any changes in amounts of loans outstanding for business purposes and for consumer credit.

7.38 With regard to government bodies, the amount of statistical and financial information made available has also been improving and at present is large and comprehensive. Although some gaps continue to exist the real problem is that of competent analysis of the information available. Here again the Association feels that further improvement will come from evolution as continuing studies are made.

RELATIVE POSITION OF THE LIFE INSURANCE COMPANIES

7.39 The life insurance companies and other collectors of savings have always had to compete with

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the numero s channels of consumer spending such as automobiles, television sets, refrigerators, washing machines and many other goods and services of a more tangible and immediate nature. Savings contracts generally have always had to be "sold" and this is particularly true of life insurance. For this purpose the life insurance companies have maintained an active group of field representatives.

7.40 The life insurance companies, of course, have been in active competition with the other financial intermediaries for the savings dollars. The record shows that over the years they have developed the largest volume of private savings although in the last decade some other financial intermediaries have been growing at a faster rate. Available information on the amounts of these savings is set out in Table 7.a.

7.41 The life insurance companies have had one distinct advantage in that they are the only industry empowered to integrate the risk of mortality with the accumulation of savings. However, life insurance contracts are usually long-term contracts and in the main are expressed in fixed-dollar amounts. Periods of price instability and particularly periods of inflation have inhibited them in competition for the available savings. During such periods the empahsis on the purchase of life insurance contracts swings away from the plans which have a high savings element to those which provide the higher degree of protection. This slows the flow of policyholder saving to the companies. At such times, contracts providing fixed guarantees lose some of their

attraction and a larger proportion of saving is diverted to the purchase of equities either directly or through mutual funds and investment trusts.

7.42 The more recent growth of investment companies and mutual funds is in part attributable to the fear engendered by post-war inflation and erosion in the purchasing power of the dollar. The same considerations have influenced the growth of trusteed and self-administered pension plans as vehicles for the accumulation of savings through partial or complete investment of such funds in equities, at a time when this avenue was closed to the life insurance companies. Legislation in 1961, however, has enabled the life insurance companies to offer this facility through segregated funds.

7.43 Years ago it was deemed desirable to supervise life insurance companies in the public interest. This supervision has helped to ensure solvency and has enhanced their ability to meet their future obligations. With regard to pension plans which are not administered by life insurance companies, the Association feels that they are equally long-term, that their activities and particularly their continuing solvency is equally important, and that in the public interest such funds should be brought under government supervision of a somewhat similar character and purpose to that of the life insurance companies. With regard to Registered Retirement Savings Plans for individuals, section 79B of the Income Tax Act makes provision for accumulation and the ultimate purchase of a life annuity. These, too, are long-term contracts, and the Association believes that in the public

[illegible]
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TABLE 7.a

Assets of Major Saving-Type Institutions in Canada

Total Assets ($000,000 omitted)

End of Year	Life Insurance Companies (1)	Charter Banks (Personal Savings)	Trusteed Pensions	Canada Savings Bonds	Trust Cos.	Invest. Cos.	Credit Unions	Mortgage Loan Cos.	Govt. Annuities	Quebec Savings Banks
1950	4,076	4,176	n.a	1,218	399	n.a.	312	n.a.	620	204
1951	4,320	4,296	n.a.	1,194	414	n.a.	359	378	676	205
1952	4,613	4,600	n.a.	1,250	432	225	424	404	737	218
1953	4,957	4,756	n.a.	1,632	440	244	489	436	798	226
1954	5,335	5,218	n.a.	2,090	588	n.a.	552	502	865	243
1955	5,724	5,633	n.a.	2,433	666	n.a.	653	559	930	265
1956	6,154	6,007	1,999	2,541	692	n.a.	761	600	989	273
1957	6,681	6,108(2)	2,460	2,469	728	n.a.	852	641	1,048	286
1958	7,142	6,844	2,791	2,895	902	550	1,009	714	1,106	303
1959	7,699	6,900	3,200	3,212	999	751	1,158	784	1,157	298
1960	8,260	7,215	3,616	3,594	1,210	900	1,299	860	1,199	311
1961 est.	8,900	7,618	4,000	4,083	1,350	1,150	1,450	940	1,236	325

Annual Changes in Assets ($000,000 omitted)

End of Year	Life Insurance Companies (1)	Charter Banks (Personal Savings)	Trusteed Pensions	Canada Savings Bonds	Trust Cos.	Invest. Cos.	Credit Unions	Mortgage Loan Cos.	Govt. Annuities	Quebec Savings Banks
1951	245	120		- 24	15		47		56	1
1952	293	304		56	18		65	26	61	13
1953	344	156		382	8	19	65	32	61	8
1954	378	462		458	148		63	66	67	17
1955	389	415		343	78		101	57	65	22
1956	430	374		108	26		108	41	59	8
1957	527	101(2)	461	108	360		91	41	59	13
1958	461	736	331	246	174		157	73	58	17
1959	557	56	409	317	97	201	149	70	51	-5
1960	561	315	416	382	211	149	141	76	42	13
1961 est.	640	403	400	489	150	250	150	80	37	15

(1) Life insurance assets held in Canada, federally-registered and provincial companies (provincial companies' assets estimated for 1951-1953).
(2) $140 million transferred out of personal savings classification.

interest vehicles through which individual accumulation under "registered" retirement savings plans takes place should be the subject of certain minimum government standards of supervision.

7.44 The conditions which will allow the life insurance companies to continue to make a maximum contribution toward the accumulation of savings and their constructive employment in the Canadian economy are:

(a) Stability in the purchasing power of the dollar and the encouragement and preservation of savings.

(b) An economic climate favourable to growth in the economy and a level of taxation which does not discourage saving.

(c) A social and political climate favourable to private individual and group action in providing for personal financial security.

(d) A basic floor of security as warranted by our ability to provide it for the aged, widows and orphans, the permanently disabled and those temporarily unemployed.

(e) Consistent protection of property rights under law, to ensure stability and confidence in financial obligations.

(f) General freedom and flexibility in investment within a minimum of statutory limitations to make possible implementation of long-term guarantees.

(g) Sound domestic environment within which all life insurance companies can operate for the benefit of Canadians and which also will facilitate effective operation of Canadian companies abroad.

APPENDIX 1

Member Companies

The Canadian Life Insurance Officers Association

Canadian

The Acadia Life Insurance Company

Aeterna-Life Mutual Assurance Company

Alliance Mutual Life Insurance Company

British Pacific Life Insurance Company

The Canada Life Assurance Company

Canadian Premier Life Insurance Company

Canadian reassurance Company

The Commercial Life Assurance Company of Canada

Confederation Life Association

The Continental Life Insurance Company

Co-operative Life Insurance Company

The Crown Life Insurance Company

Desjardins Mutual Life Assurance Company

The Dominion Life Assurance Company

The Dominion of Canada General Insurance Company

The T. Eaton Life Assurance Company

L'Economie Mutuelle d'Assurance

The Empire Life Insurance Company

The Equitable Life Insurance Company of Canada

The Excelsior Life Insurance Company.

Fidelity Life Assurance Company

Global Life Insurance Company

The Great-West Life Assurance Company

APPENDIX 1

Member Companies

The Canadian Life Insurance Officers
[illegible]

[illegible]

[illegible]

[illegible]

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The Dominion Life Assurance Company

The Dominion of Canada General Insurance Company

The T. Eaton Life Assurance Company

L'Economie Mutuelle d'Assurance

[illegible]

The Equitable Life Insurance Company of Canada

The Excelsior Life Insurance Company.

[illegible]

[illegible]

The Great-West Life Assurance Company

The Imperial Life Assurance Company of Canada
The Industrial Life Insurance Company
The Laurentide Life Assurance Company
The Life Insurance Company of Alberta
The London Life Insurance Company
The Manufacturers Life Insurance Company
The Maritime Life Assurance Company
The Monarch Life Assurance Company
Montreal Life Insurance Company
The Mutual Life Assurance Company of Canada
La Mutuelle-Vie de l'U.C.C.
The National Life Assurance Company of Canada
North American Life Assurance Company
The Northern Life Assurance Company of Canada
Les Prevoyants du Canada
The Provident Assurance Company
The Quebec Mutual Life Assurance Company
La Sauvegarde Life Insurance Company
La Solidarite Life Assurance Company
The Sovereign Life Assurance Company
Sun Life Assurance Company of Canada
La Survivance Mutual Life Assurance Company
Toronto Mutual Life Insurance Company
Union of Commerce Mutual Life Insurance Company
The Union Life
The Wawanesa Mutual Life Insurance Company
The Western Life Assurance Company

The Imperial Life Assurance Company of Canada

[illegible]

The Laurentide Life Assurance Company

The Life Insurance Company of Alberta

[illegible]

The Manufacturers Life Insurance Company

[illegible]

The Monarch Life Assurance Company

[illegible]

The Mutual Life Assurance Company of Canada

La Mutuelle-Vie de l'U.C.C.

The National Life Assurance Company of Canada

[illegible]

The Northern Life Assurance Company of Canada

Les Prevoyants du Canada

[illegible]

The Quebec Mutual Life Assurance Company

La Sauvegarde Life Insurance Company

[illegible]

The Sovereign Life Assurance Company

[illegible]

La Survivance Mutual Life Assurance Company

Toronto Mutual Life Insurance Company

Union of Commerce Mutual Life Insurance Company

[illegible]

[illegible]

The Western Life Assurance Company

British

Commercial Union Assurance Company Limited

Co-operative Insurance Society Limited

The London Assurance

London and Scottish Assurance Corporation, Limited

The Mercantile and General Reinsurance Company Limited

The Mutual Life and Citizens' Assurance Company Limited

The Norwich Union Life Insurance Society

Pearl Assurance Company, Limited

Phoenix Assurance Company Limited

The Prudential Assurance Company Limited (of England)

Royal Insurance Company, Limited

The Standard Life Assurance Company

The Victory Insurance Company Limited

Dutch

Holland Life Insurance Society Limited

German

Concordia Life Insurance Company

Munich Reinsurance Company

United States

Aetna Life Insurance Company

Bankers Life Company

Business Men's Assurance Company of America

Connecticut General Life Insurance Company

Continental Assurance Company

Cuna Mutual Insurance Society

The Equitable Life Assurance Society of the U.S.

Federal Life and Casualty Company

Hartford Life Insurance Company

John Hancock Mutual Life Insurance Company

The Lincoln National Life Insurance Company

Loyal Protective Life Insurance Company

Massachusetts Mutual Life Insurance Company

Metropolitan Life Insurance Company

The Ministers Life and Casualty Union

The Minnesota Mutual Life Insurance Company

The Mutual Life Insurance Company of New York

New England Mutual Life Insurance Company

New York Life Insurance Company

North American Life and Casualty Company

North American Reassurance Company

Occidental Life Insurance Company of California

Old Republic Life Insurance Company

Pacific Mutual Life Insurance Company

The Paul Revere Life Insurance Company

Presbyterian Ministers' Fund

Provident Life and Accident Insurance Company

The Prudential Insurance Company of America

State Farm Life Insurance Company

State Mutual Life Assurance Company of America

The Travelers Insurance Company

Union Mutual Life Insurance Company

United Benefit Life Insurance Company

Washington National Insurance Company

APPENDIX 2

Special Committee

Appointed to Prepare a Submission to the Royal Commission on Banking and Finance

Chairman - J.T. Bryden
North American

Members -

A.H. Lemmon, Canada
P.S. Bower, Great-West
A.R. Poyntz, Imperial
S.E. Brock, Industrial
R.H. Reid, London
G.L. Holmes, Manufacturers
G.R. Berry, Metropolitan
E.A. Rieder, Mutual of Canada
J.A. Rhind, National
J.J. Wilson, Prudential of America
G.T. Westwater, Standard
E.R. Alexander, Sun

Secretary - F.C. Dimock
C.L.I.O.A.

Officers of the Association

1962-63

President - E.A. Rieder, The Mutual Life Assurance Company of Canada

First Vice President - B.T. Holmes, Confederation Life Association

Second Vice President - H.L. Sharpe, The Northern Life Assurance Company of Canada

Honorary Treasurer - M.K. Kenny, The Excelsior Life Insurance Company

Past President - J.T. Bryden, North American Life Assurance Company

302 Bay Street
Toronto, Canada

John A. Tuck, Q.C.,
Managing Director & General Counsel.

APPENDIX 3

Note re Tables 4.a and 4.b on Estimated Life Insurance Saving in Canada

The original concept of life insurance saving was developed by Simon A. Goldberg, Assistant Dominion Statistician, in his doctoral thesis for Harvard University. Basically, life insurance saving is defined as receipts in Canada minus disbursements in Canada. For details, see the publication of the Dominion Bureau of Statistics entitled "National Accounts, Income and Expenditure, Preliminary, 1949", page 13 et seq.

The series for 1954 - 1960 has been calculated by The Canadian Life Insurance Officers Association largely on Dr. Goldberg's model.

Certain calculations involve arbitrary breakdowns:

For Canadian federally-registered companies:

The following methods are used to estimate in-Canada figures where no actual figures are available:

(1) Considerations for settlement annuities are split on the ratio of settlement annuities effected in Canada to total settlement annuities effected.

(2) Deposits left with the companies are split on the mean of (a) the ratio of dividends left on deposit in Canada to total dividends left on deposit and (b) the ratio of the liability for accumulated amounts on deposits in Canada to the liability for total amounts on deposit.

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(3) Investment income and expenses are split on the ratio of actuarial reserves in Canada to total actuarial reserves.

(4) Payments under settlement annuities are split on the ratio of settlement annuities in force in Canada to total settlement annuities in force.

(5) Staff welfare expenses are split on the actuarial reserve ratio (see 3). Other expenses are split on the ratio of sales and business in force in Canada to total sales and business in force with sales weighted ten-fold.

For Provincial companies:

Expenses are calculated as a fixed percentage of premium income. This percentage is based on a detailed analysis of the 1958 operations of 11 provincial companies.

For Non-Canadian companies:

An arbitrary 10 per cent is added to expenses reported in respect of Canadian operations as "head office expense" on the following ground: The companies' Canadian annual statements do not include some or all head office expenses but the premiums charged in Canada presumably do. Therefore, it is argued, the saving of Canadian policyholders would be over-stated if an allowance for these head office expenses were not made. No reverse allowance is made in respect of the business outside Canada of the Canadian companies.